

COMMONWEALTH OF PENNSYLVANIA



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August 14, 1995

John G. Alford, Secretary
PA Public Utility Commission
Room G-23, North Office Bldg.
Harrisburg, PA 17105-3265

Re: PA Public Utility Commission
v. Pennsylvania Power & Light
Company, Docket No. R-00943271

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Dear Secretary Alford:

Enclosed please find for filing an original and nine copies of the Office of Consumer Advocate's Exceptions in the above-captioned proceeding.

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

Sincerely,


Mary C. Kenney
Assistant Consumer Advocate

Enclosures

cc: All parties of record
Hon. Robert A. Christianson, ALJ
Cheryl Walker Davis, Esq. (OSA)

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY
COMMISSION

v.

Docket No. R-00943271

PENNSYLVANIA POWER & LIGHT
COMPANY

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EXCEPTIONS
OF THE
OFFICE OF CONSUMER ADVOCATE

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DOCKETED
AUG 15 1995

For:

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Dated: August 14, 1995

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I. INTRODUCTION

The Office of Consumer Advocate (OCA) hereby submits the following Exceptions to the Recommended Decision of Acting Chief Administrative Law Judge Christianson, issued July 31, 1995, in the above-captioned matter.

II. EXCEPTIONS

EXCEPTION 1: Excess Capacity (R.D. 11 to 30)

A. Introduction

At pages 11 to 30, the ALJ discusses the issue of excess capacity on the PP&L system. In his discussion, the ALJ finds that Section 1323 of the Public Utility Code, 66 Pa.C.S. § 1323, does not apply to PP&L's claim to earn, for the first time, an equity return on Susquehanna 2. R.D. at 26. As a result, the ALJ does not analyze whether Susquehanna 2 constitutes economic excess capacity. Rather, the ALJ considers the issue of whether PP&L has more megawatts of capacity than necessary to provide reliable service, basing the analysis on what the ALJ termed the "classic test" of physical excess capacity. R.D. at 27.

In applying this physical excess capacity test, the ALJ correctly found that PP&L had substantial physical excess capacity on its system. The OCA, however, would recommend an alternative approach to the analysis than that adopted by the ALJ, as discussed below. The OCA excepts, however, to the ALJ's failure to consider the issue of economic excess capacity pursuant to Section 1323 or general "used and useful" principles.

B. Physical Excess Capacity

The ALJ, in his Recommended Decision, found that PP&L had 564 MW of physical excess capacity. The ALJ, in making his finding, adopted the Office of Trial Staff's analysis of physical excess capacity. The OCA concurs with the ALJ's conclusion that PP&L has physical excess capacity. The OCA would note, however, that the OCA's analysis, which looked at the test year and the year following the test year, also demonstrated that PP&L has physical excess capacity in the range of 400 MW to 800 MW. See, OCA M.B. at 30-45 and OCA R.B. at 13-22.¹

The ALJ adopted the analysis performed by OTS witness Metro in making his recommendation. In addition, the ALJ adopted the 16% reserve margin recommended by OTS witness Metro. Mr. Metro's analysis develops a nine year average of excess available resources in determining the level of physical excess capacity. OTS St. 5 at 21-22. The OCA submits that, pursuant to Section 1323(a) of the Public Utility Code, and Commission precedent, the Commission has also utilized a physical excess capacity test that looks at the Company's capacity resources in the test year and the year following the test year. See, 66 Pa.C.S. § 1323(a);² Pa. P.U.C. v. PECO, 54 Pa. PUC 220, 226 (1980).

As noted above, the OCA presented an analysis of whether PP&L has physical excess capacity by comparing the PP&L's installed and available capacity resources to PP&L's peak customer demand plus a reasonable reserve margin in the test year and the year following the

¹ The OCA does not except to the ALJ's finding. The OCA submits this discussion in order to provide an alternative method of analysis of physical excess capacity for the PUC to consider.

² The OCA discusses the applicability of Section 1323 below.

test year. Using a 12% to 15% reserve margin range determined by OCA witness Kahal to be reasonable for PP&L for the purposes of this proceeding,³ and utilizing PP&L's own determination of its resources, including the NUG capacity, Mr. Kahal determined that PP&L has physical excess capacity of between 400-800 MW. OCA St. 2 at 16. See, OCA M.B. at 30-46 and R.B. at 13-22.

The OCA submits that Mr. Kahal's analysis is reasonable and provides a basis for determining excess capacity pursuant to Section 1323 and the Commission's prior decisions. As such, the OCA submits that Mr. Kahal's analysis, and reserve margin range, should be considered in support of the need for a physical excess capacity adjustment in this proceeding.

C. Economic Excess Capacity

1. Section 1323 Applies To The Company's Claim.

The OCA submits that the ALJ erred in finding that Section 1323 does not apply to the Company's claim to earn, for the first time, an equity return on Susquehanna 2. R.D. at 26-27. The ALJ concludes that PP&L is "not claiming the cost of Susquehanna 2 for the first time in this proceeding" and thus does not apply the excess capacity tests provided for in that Section. R.D. at 26-27. The ALJ reasons that since PP&L received partial recognition of Susquehanna 2 in the last case, that Section 1323 does not apply. Id. The ALJ also expresses concern that the "details of Section 1323 really do not work when we are dealing with a timeframe 10 years

³ As the OCA set forth fully in its testimony and Briefs, the 12% to 15% reserve margin range is reasonable for an analysis of PP&L's resources in the test year and the year following. The lower bound of 12% represents the reserve margin assigned by PJM to PP&L, and is utilized by PP&L in its own reliability planning. OCA St. 2A at 9. The upper bound of 15% provides a 3%, or 200 MW cushion to account for the imperfections of capacity planning. OCA St. 2 at 14-16.

after the completion of the project." Id.

As the OCA set forth fully in the OCA's Main Brief at pages 21-27, and its Reply Brief at pages 9-13, Section 1323 applies to the Company's claim to earn, for the first time, a return on common equity associated with Susquehanna 2. The ALJ bases his decision on the Company's argument that since it had previously attempted to claim Susquehanna 2 in rates in 1985 and received recognition of many of these costs in rates, its claim in this case does not constitute its first claim. The OCA submits, however, that the ALJ's recommendation is contrary to Commission precedent and sound public policy.

Section 1323(a), in pertinent part, states that "[w]hen a public utility claims the costs of an electric generating unit in rates for the first time and the commission finds that the unit results in the utility having excess capacity, the commission shall disallow . . ." 66 Pa.C.S. § 1323(a). The Commission has previously interpreted this language to relate to generating facilities that had not previously been recognized in rates--even where the utility had previously sought such recognition. Indeed, any other holding would suggest that Section 1323 is only effective for nine months, that is, the time it takes a utility to get through a rate case. Once that rate case was completed, regardless of the result, Section 1323 would become meaningless.

In Pennsylvania Public Utility Commission v. West Penn Power Company, 61 Pa. PUC 711, 77 PUR 4th 220 (1986), the Commission considered West Penn's request for ratemaking recognition of the Bath County Pumped Storage Project. West Penn had first sought rate recognition of the Bath County project in its previous base rate case filed in 1984, but such recovery was denied because the unit did not enter commercial service during the test year.

In the next base rate case, decided in 1986 after the enactment of Section 1323, West

Penn again sought ratemaking recognition of the Bath County Project. The Commission found that Section 1323 would apply to the Company's claim, even though the costs of Bath County had been previously claimed by the Company. West Penn 1986, 61 Pa. PUC at 736-37.

The Commission has applied Section 1323 on at least two other occasions despite the fact that the utility involved had claimed the costs associated with the generating facility at issue in a previous proceeding. See, Pennsylvania Public Utility Commission v. Duquesne Light Company, 63 Pa. PUC 337 (1988) and Pennsylvania Public Utility Commission v. Pennsylvania Power Company, 64 Pa. PUC 308 (1988). The OCA submits that the Commission's interpretation of the applicability of Section 1323 as set forth in these cases is reasonable and should be applied to PP&L's claim to earn, for the first time, a return on equity associated with Susquehanna 2. Any other interpretation of Section 1323 would produce an absurd result.

For example, if Section 1323 was intended to only apply to the first time a utility claimed the costs of a generating plant, a utility could reverse any excess capacity disallowance by merely filing another base rate case one day after the Commission's order was entered in its first case. Under that interpretation, regardless of the extent of physical or economic excess capacity, the utility could avoid the legal standards set forth in Section 1323 by filing a second case immediately. Such an interpretation would produce an absurd result, and one that does not favor the public interest. As the Commission has previously recognized:

[T]he General Assembly would: (1) not intend an absurd result, and (2) would intend to favor the public interest as opposed to the private interest. 1 Pa.C.S. § 1922.

Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 74 Pa. PUC 1, 131 (1990).

As noted in the OCA's Main Brief and Reply Brief, the legislative history of Section 1323 confirms that the General Assembly intended that Section 1323 would apply to PP&L. In considering an amendment to HB 1639, PN 3778, which related to cogeneration projects on a utility's system and was subsequently embodied in Section 1323(c), Representative Laughlin stated:

Mr. Speaker, the last thing that this particular legislation does that was not previously there is that it gives a window for a cogeneration project of culm banks in the PP&L (Pennsylvania Power & Light Company) area of northeastern and central Pennsylvania.

Legislative Journal of Pennsylvania House of Representatives, Report to the General Assembly on June 25, 1986, at 1554 (Vol. II, 1986).

Indeed, the OCA submits that a review of Section 1323(c) reveals that it clearly applies to units that were in commercial operation before the law was enacted, such as Susquehanna 2. Section 1323(c), in relevant part, provides:

. . . in determining whether a base load unit, which was in commercial operation for at least one year prior to the effective date of this section, results in a public utility having excess capacity. . .

66 Pa.C.S. § 1323(c).

The OCA submits that, in accordance with prior precedent, the Commission must apply Section 1323 to the Company's claim to recover, for the first time in rates, an equity return on its investment associated with Susquehanna 2. For the Commission to find otherwise would produce the absurd result that a utility could reverse a Commission imposed excess capacity adjustment by merely filing another base rate case at any time following the Commission's initial order. The OCA submits that such a result would be contrary to the public interest and the clear legislative intent of the statute.

2. Economic Excess Capacity Is A Relevant Consideration Under A Traditional Used And Useful Analysis.

Rather than apply Section 1323, the ALJ evaluated PP&L's claims in this case utilizing the "used and useful" principle. The OCA submits, however, that the ALJ has erred in concluding that the used and useful principle, as set forth in Commission precedent, does not include an analysis of economic excess capacity.

Even before Section 1323 was enacted, the Commission has considered evidence regarding whether a generating facility would produce net economic benefits when analyzing the used and useful nature of these facilities. In a 1987 case involving Duquesne Light Company, the Commission summarized the principles that had been established in its pre-1986 precedent regarding excess capacity adjustments as follows:

These adjustments were made to balance the risks associated with bringing new generating plant on line between the utility's shareholders and ratepayers. The test used by the Commission in making these adjustments were whether: a) the investments in the plants were prudent when made, and (b) would the plants be used and useful during the period when rates will be in effect. In addition, the Commission also considered evidence as to whether the plants would produce net economic benefits. *PECO, PP&L, I, and PP&L, II.*

Pennsylvania Public Utility Commission v. Duquesne Light Company, 66 Pa. PUC 518, 623 (1988).

Notably, in PP&L's last base rate case, prior to the enactment of Section 1323, the Company itself encouraged the Commission to consider the economic benefits of Susquehanna

2. Pennsylvania Public Utility Commission v. Pennsylvania Power & Light, 59 Pa. PUC 332, 347 (1985). Based on the evidence adduced in that case, the Commission held:

Second, and even more important, we hold that even on the Company's best case, future economic benefits will not accrue until the next decade.

Id. at 348.

The Commission also considered the issue of the economic benefit of Susquehanna 1 when the Company claimed the costs of that unit in rates in its base rate case filed in 1982. Pennsylvania Public Utility Commission v. Pennsylvania Power & Light Company, 57 Pa. PUC 559, 576 (1983). As to Susquehanna 1, the Commission concluded:

In the final analysis, the ALJ properly concludes that while the economic viability studies are unresponsive of the inclusion of the excess capacity in rate base, these studies clearly support the ultimate conclusion that from an economic perspective the company indeed has excess capacity.

Id. at 576. In that case, the Commission disallowed a return on 945 MWs of PP&L's net plant investment. Id. at 578.

The OCA submits that the ALJ erred in failing to consider the evidence regarding economic excess capacity even when conducting an analysis under the traditional "used and useful" principle. The Commission considered such evidence before the enactment of Section 1323, and Section 1323 itself relies upon the Commission's precedent regarding the used and useful principles. The Company provided no reason as to why its claim for a return on common equity associated with Susquehanna 2 should be exempt from such review. Indeed, a brief review of the economic evidence, as set forth below, demonstrates the substantial economic penalty to PP&L's ratepayers associated with Susquehanna 2.

3. Economic Excess Capacity Analysis

The OCA discussed the issue of economic excess capacity extensively in its Main Brief (Proprietary and Non-Proprietary versions) at pages 46-59, and in its Reply Brief at pages 22-30. The OCA will not repeat that discussion here. The OCA will, however, briefly outline its economic excess capacity analysis since the ALJ did not discuss this issue in his Recommended

Decision.

The economic test for excess capacity as set forth in Section 1323 is as follows:

For purposes of this section, a rebuttable presumption is created that a unit or units or portion thereof shall be determined to be excess unless . . . if it is a base load unit, it is also found to produce annual economic benefits which will exceed the total annual cost of the plant during the test year or within a reasonable period following the test year.

66 Pa.C.S. § 1323(a).

The OCA presented the testimony of Matthew I. Kahal on the issue of both physical and economic excess capacity. After a review of the evidence in this case, Mr. Kahal testified:

Based on my review of the evidence, I conclude that Susquehanna 2 is economic excess capacity. The Susquehanna plant does not provide economic benefits in excess of its current revenue requirement to ratepayers. The Company's own study indicates that Susquehanna's revenue requirement cost will exceed the market cost of power during at least the next ten years, and on a cumulative present value basis would result in a net economic detriment . . .⁴

OCA St. 2 at 4. As the OCA noted in its Main Brief, this economic excess capacity problem is even more compelling today than it was when the Commission first considered the issue as to Susquehanna 2 in 1984.⁵ OCA witness Kahal explained:

At the time of the last rate case, the Company argued Susquehanna would be an economically attractive resource on a life cycle basis. It is clear from my review of the discovery documents that this is no longer PP&L's assessment--absent substantial improvements in the plant's performance and cost control. Whether

⁴ The amount of the loss is proprietary, but is set forth in the proprietary version of OCA St. 2 at 4, as well as in the proprietary version of the OCA's Main Brief at pages 46 to 55.

⁵ At page 26 of his Recommended Decision, the ALJ states that the situation has changed in the ten years since PP&L's last rate case. From this, the ALJ concludes that the OCA's recommendation, which he characterizes as one to maintain the status quo, should not be adopted. The OCA submits, however, that the change which the ALJ has referred to has been one to the detriment of ratepayers. Indeed, the change makes it even more compelling for the Commission to adopt an excess capacity adjustment related to Susquehanna 2.

PP&L can attain such improvements is uncertain and, more importantly, these cost savings are not reflected in PP&L's request in this case.

OCA St. 2 at 5.

OCA witness Kahal presented an analysis of whether Susquehanna 2 produces economic benefits for ratepayers within a reasonable period of time. In conducting this analysis, Mr. Kahal compared the full revenue requirement cost of Susquehanna 2 with the market price of power supply over a five to ten year time frame. OCA St. 2 at 17. In addition, Mr. Kahal examined evidence regarding life cycle comparisons, and the Company's own study, Strategy 2000. Mr. Kahal's analysis is discussed thoroughly in the OCA's M.B. at pages 47-55 and its Reply Brief at 22-28.

In making his analysis, Mr. Kahal first determined the cost of power from Susquehanna 2 on a revenue requirements basis using a range of parameters for possible disputed items such as the rate of return, decommissioning and depreciation. Within these parameters, and assuming that the plant operates at a capacity factor of 75% to 80%, the average cost for Susquehanna 2 is 5.67¢/kwh to 6.37¢/kwh. OCA St. 2 at 20. This range is consistent with, and even somewhat lower than, the 6.7¢/kwh average cost utilized by PP&L witness Hieronymus in his study. Tr. 2352. In order to simplify the comparison, Mr. Kahal utilized an average cost of 6.0¢/kwh. Id.

OCA witness Kahal then assessed the probable market cost of power over the next five to ten years by examining several sources of information, both confidential and non-confidential, supplied by PP&L. Based on his review of this evidence, Mr. Kahal determined that a reasonable range of probable market costs of "all hours" base load power is in the range of 2.5¢/kwh to 5.0¢/kwh over the next ten years, with a five to ten year average of 3¢/kwh to

4¢/kwh. OCA St. 2 at 20.

By then comparing the 6¢/kwh cost of Susquehanna 2 to the market cost of 3¢/kwh to 4¢/kwh, it is clear that Susquehanna 2 does not produce net economic benefits to ratepayers within a reasonable time frame. Using a five year perspective, Mr. Kahal determined that the revenue requirement cost of Susquehanna 2 is about \$150 to \$200 million per year above market.⁶ OCA St. 2 at 6. The OCA submits that based on these facts, the Commission must find that Susquehanna 2 constitutes economic excess capacity.⁷

D. Remedy

After finding that the Company has physical excess capacity, the ALJ recommends a disallowance based on a 564 MW slice of PP&L's system. R.D. at 28-30. The ALJ rejected the OCA's recommended adjustment which continued the Commission's previous disallowance of the return on common equity associated with Susquehanna 2. In rejecting the OCA's recommendation, the ALJ reasons that the situation has somewhat changed from ten years ago, and we should not merely repeat the disallowance of the last case. R.D. at 26. Moreover, the

⁶ The Company has argued against the use of current market information in the economic excess capacity test. The OCA has addressed these arguments in both its Main Brief at pages 47 to 50, and its Reply Brief at 24 to 28, and will not repeat those arguments here. The OCA would note, however, that as competition in the generation market increases, timely and reliable information is now available to the Commission for assessing whether a baseload unit will provide net economic benefits to ratepayers within a reasonable time.

⁷ In rebuttal, PP&L presented a "coal proxy" type analysis where the year by year revenue requirements of Susquehanna 2 were compared to the year by year revenue requirements of a new coal plant entering service in 1995. PP&L St. 16-R at 55-56. The OCA submits that this analysis does not provide a meaningful method of analyzing the issue of whether Susquehanna 2 constitutes excess capacity. Notably, the construction of a new coal plant is not supported by PP&L's own planning reports. Thus, the PP&L analysis merely compares Susquehanna 2 to what the Company has determined to be an uneconomic resource. The OCA discussed this issue in its Main Brief at 55-59 and its Reply Brief at 28-30.

ALJ reasons that the current overcapacity situation is produced by the entire PP&L system, not just Susquehanna 2. R.D. at 28.

The OCA submits that its recommendation to disallow the return on common equity associated with Susquehanna 2 is reasonable and appropriate given the substantial net economic penalty for PP&L's ratepayers associated with Susquehanna 2. As the Commission recognized in PP&L's last rate case, where it first disallowed the equity return on Susquehanna 2, such a disallowance constituted a fair sharing of the costs of this excess capacity. The Commission stated:

The common shareholders assumed the risk that the investment in SSES 2 would succeed, and this risk has presumably been reflected in their authorized rate of return. Even though there has been no finding of imprudence, that risk remains on the shareholders. This is not a penalty, but rather a proper allocation of risk and its consequences.

PP&L 2, 59 Pa. PUC at 351.

The Commission, based on the evidence adduced in that case, also recognized that PP&L's excess capacity problem would extend far into the future. As the Commission stated:

Second, and even more important, we hold that even on the Company's best case, future economic benefits will not accrue until the next decade. The sheer magnitude of the delay combined with the uncertainty of the projections render the net present value approach meaningless on the record before us.

Id. at 348.

The OCA submits that the future is here, and the record in this case demonstrates that Susquehanna 2 still does not produce net economic benefits to ratepayers. Although the ALJ reasons that much has changed, the OCA submits that one important point remains the same-- Susquehanna 2 does not produce net economic benefits to ratepayers now, or in the reasonably foreseeable future. The OCA submits that the Commission's disallowance set forth in PP&L's

previous proceeding should not be reversed, or modified, until such time as the Company can show that Susquehanna 2 is fully used and useful in service to the public, a showing not made on this record.

Indeed, the Commonwealth Court recognized this principle when it upheld the Commission's disallowance of an equity return on Susquehanna 2 as a proper balancing of the interests of ratepayers and shareholders. Pennsylvania Power and Light Co. v. Pennsylvania Public Utility Commission, 101 Pa. Commw. 370, 516 A.2d at 431-32 (1986).

The OCA submits that the continuation of the equity disallowance on Susquehanna 2 is reasonable based on the facts of this case. OCA witness Kahal assessed the effect of the continuation of this disallowance as follows:

Thus, with the common equity return disallowance, there is roughly a 50/50 sharing between ratepayers and investors of the uneconomic costs for Unit 2. However, following that perspective implies that ratepayers absorb 100 percent of the Unit 1 uneconomic costs. Alternatively, spreading the \$62 million disallowance over both units, ratepayers absorb 75 percent and shareholders only 25 percent of the uneconomic costs.

OCA St. 2 at 23.

As noted above, the OCA's recommended disallowance, based on its return on equity recommendation of 11.1% and an equity ratio of 45%, is \$61.85 million on a Pennsylvania jurisdictional basis. OCA St. 2 at 21. The final disallowance, however, must be consistent with the Commission's rulings on return on equity, capital structure, rate base adjustments and jurisdictional allocation percentage.

For the reasons set forth above, and the reasons set forth in the OCA's Main Brief at 11-63 and Reply Brief at 7-31, the OCA submits that the Commission should continue the return on equity disallowance associated with Susquehanna 2 that was established by the Commission

in PP&L's last rate case.

EXCEPTION 2: Accrued Pensions (R.D. at 32)

The ALJ recommended that the OCA's adjustment deducting the balance of the accrued pension liability from rate base should be rejected, reasoning that the OCA seems "to be suggesting an adjustment clause, similar to the ECR." R.D. at 32. The OCA submits that this is a mischaracterization of its adjustment in this proceeding, and thus excepts to the ALJ's recommendation. As set forth in the OCA's Briefs, the OCA is not seeking a "true-up" of PP&L's pension expense. Rather, the OCA's adjustment reflects that these funds have already been recovered from ratepayers, but not yet contributed to PP&L's pension fund. OCA M.B. at 65-67; OCA R.B. at 39-41. As such, these ratepayer funds should be reflected as a reduction to PP&L's current rate base.

As OCA witness Catlin explained, the accrued pension liability which is reflected on PP&L's books represents the difference between the pension costs which have been reflected on PP&L's books and the Company's contributions to its pension fund since the implementation of Statement of Financial Accounting Standard ("SFAS") No. 87 in 1987. OCA St. 6 at 5. Mr. Catlin testified:

Since 1987, the pension costs recorded on the Company's books have either already been recovered from ratepayers as an expense in the year in which they were recorded or are being recovered as a component of the capitalized overheads included in the cost of plant in service. Therefore, the accrued pension liability represents funds that have been recovered from ratepayers, but which have not been contributed to the pension fund by the Company.

Id. The OCA submits that the balance of the accrued pension liability should be deducted from rate base to reflect the fact that ratepayers have paid these pension costs although they have not yet been contributed to the Company's pension fund. For the reasons set forth above and in the

OCA's Main and Reply Briefs, the OCA submits that the ALJ's recommendation should be rejected, and the OCA's adjustment to PP&L's rate base which recognizes the Company's accrued pension liability should be accepted. Adoption of the OCA's adjustment reduces total Company rate base by \$85,537,00 and Pennsylvania jurisdictional rate base by \$74,034,000. OCA St. 6, Sch. TSC-3.

EXCEPTION 3: Cash Working Capital (R.D. at 34)

A. Introduction

In this proceeding, PP&L's own calculations result in a negative cash working capital ("CWC") requirement, although PP&L has chosen to set its CWC requirement at zero. PP&L St. 3R at 2. Both the OTS and OCA recommended a negative CWC requirement due to the fact that setting the CWC requirement at zero ignores the fact that ratepayers are supplying more funds to the Company than are required. However, the ALJ rejected these recommendations, finding that the "interest/dividend offset should only be used against a positive cash working capital." R.D. at 35. As a result of this finding, the ALJ did not address the OCA's adjustments to the Company's CWC calculation, including adjustments to PP&L's expense lag and balance of prepayments. OCA M.B. at 75-85; OCA R.B. at 35-39. The OCA submits that the ALJ's recommendation should be rejected and that the Commission should treat positive and negative cash working capital requirements in the same manner.

B. The Commission Should Recognize Negative CWC In This Case.

In this proceeding, the ALJ accepted PP&L's argument that the interest dividend offset "should only be used against a positive cash working capital balance." R.D. at 35. The OCA submits that this finding fails to consider the effect on ratepayers of a negative cash working

capital requirement. As Mr. Catlin explained:

A negative cash working capital requirement signifies that, on average, the Company is recovering the revenues which it receives for providing service prior to the time that it must pay for the expenses incurred to provide service. A negative cash working capital requirement indicates that PP&L has the use of ratepayer supplied funds to offset other working capital requirements.

OCA St. 6A at 8. The OCA submits that PP&L's ratepayers are entitled to recognition of the funds supplied in excess of that required by the Company's cash working capital requirement.

As discussed in the OCA Briefs, the OCA recognizes that this Commission has in the past set the cash working capital allowance at zero rather than adopting a negative cash working capital determination.⁸ OCA M.B. at 72-73; OCA R.B. at 33-34. However, the Commission has also allowed negative cash working capital allowances. See Pa. P.U.C. v. ALLTELL Pennsylvania, 59 Pa. PUC 447, 457-58 (1985). Here, the Company's negative cash working requirement is caused by the offset for the lag in the payment of bond interest and preferred dividends. The Commission has long held that these funds should be deducted from CWC. This adjustment is independent of other aspects of CWC. See, Pa. P.U.C. v. Pennsylvania Power & Light Company, 54 Pa. PUC 645, 655 (1981); Pa. P.U.C. v. Pennsylvania Power Company, 55 Pa. PUC 552 (1982). OCA M.B. at 72.

The OCA submits that ratepayers would be doubly harmed by the adoption of the ALJ's recommendation to set PP&L's cash working capital requirement at zero. First, it ignores the long standing precedent deducting accumulated debt interest and preferred stock funds dividends

⁸ See Pa. P.U.C. v. Equitable Gas Company, 60 Pa. PUC 127, 140-141 (1985); Pa. P.U.C. v. Pennsylvania Power Company, 64 Pa. PUC 308, 342 (1988); Pa. P.U.C. v. Duquesne Light Company, 66 Pa. PUC 518, 654 (1988); Pa. P.U.C. v. Pennsylvania Power Company, 67 Pa. PUC 91, 342 (1988).

from cash working capital. Second, it allows PP&L the use of ratepayer supplied funds to offset other working capital requirements. The Commission's past practice of setting cash working capital allowances at zero should not preclude the allowance of long established cash working capital adjustments. Accordingly, the OCA's adjustment should be adopted.

C. The OCA's Adjustments to Cash Working Capital.

As discussed above, the OCA submits that the ALJ erred in setting the Company's CWC claim at zero. In addition, by not addressing the Company's actual negative cash working capital allowance, the ALJ failed to consider the adjustments proposed by the OCA to correct errors in the Company's CWC calculation. As set forth in the OCA's Main and Reply Briefs, the OCA proposed three adjustments to the Company's lead/lag study. The three adjustments included: removing the CAAA permit fees and interest on customer deposits from the O&M expense lag;⁹ excluding the Sunbury pump invoice from the O&M expense lag since it was a capitalized item;¹⁰ and adjusting the expense lags associated with interest on long-term debt and preferred stock dividends to correct an error in the Company's payment lag computation. OCA M.B. at 75-82. In addition, OCA witness Catlin proposed an adjustment to reduce the Company's balance of prepayments to eliminate the balance of prepaid insurance and the effects of the one-day prepayment of interest and preferred dividends. This adjustment eliminates a double count resulting from the inclusion of the balance of prepaid insurance in rate base and

⁹ The Company contested the CAAA permit fee adjustment. The OCA submits that this adjustment is proper since these fees have a payment lag of approximately 14 months (See, Pa. P.U.C. v. West Penn Power Co., Docket No. R-00942986, slip op. at 18 (December 28, 1994).

¹⁰ See, Pa. P.U.C. v. National Fuel Gas Distribution Co., 62 Pa. PUC 407, 414-415 (1986).

the inclusion of insurance premiums in the lead/lag study. OCA M.B. at 78-85; OCA R.B. at 35-39. An adjustment to the revenue lag to correct the 20-day account lag was accepted by the Company in rebuttal.

The OCA submits that the Commission must reject the ALJ's recommendation to set PP&L's CWC at zero and find that the Company has a negative cash working capital, including the adjustments set forth above. See, OCA M.B. at 67-85; R.B. at 32-39.

EXCEPTION 4: Early Retirement Program (R.D. at 44-45)

In this proceeding, PP&L requested that it be allowed to defer and amortize the costs associated with the Voluntary Early Retirement Program ("VERP") which it offered in late 1994. The Company is requesting a five year amortization of the \$75,859,000, a cost of \$15,172,000 per year. PP&L St. 2 at 12-14, PP&L Exh. Future 1 (Revised), Sch. D-10. The OCA supported the adjustment proposed by PPLICA witness Lane Kollen to reduce the amount of the costs which PP&L is allowed to amortize by netting out the savings which PP&L will realize from the VERP prior to the time the savings are reflected in rates. OCA M.B. at 158-158; OCA R.B. at 73-74. The ALJ recommended the rejection of this adjustment finding that although he agreed that "some of the cost increases associated with the recent months might not be continued over the long term", he found "no good basis for adding the short term information for creation of an adjustment." R.D. at 44.

The OCA submits that the ALJ's denial of this adjustment fails to recognize that PP&L seeks to recover the gross cost of the VERP from December 31, 1994 to September 30, 1995 despite the fact that it was also the beneficiary of nine months of VERP savings in this time period. OCA M.B. at 158-159; OCA R.B. at 73-74. As OCA witness Catlin testified:

In developing its adjustment, PP&L has recognized that the VERP will produce ongoing cost savings during the period the rates approved in this case will be in effect. However, the Company has not recognized the VERP will have produced cost savings prior to the time the VERP is reflected in rates just as costs were incurred prior to the time the VERP is reflected in rates.

OCA St. 6A at 6; OCA M.B. at 159. The OCA submits that the ALJ's recommendation results in a mismatch between the costs and benefits of the program. PP&L should not be allowed to defer the costs of the program for future rate recovery without also recognizing that the VERP has produced cost savings which were not reflected in rates. Thus, the adjustment proposed by Mr. Kollen to net out the cost savings realized prior to the end of the test year from the VERP costs to be amortized is necessary and appropriate. Adoption of this adjustment reduces test year expenses by \$5,799,000 on a total company basis and \$5,019,000 on a jurisdictional basis compared to PP&L's revised claim. The corresponding increases in net income are \$3,355,000 and \$2,904,000, respectively. See OCA St. 6A, Sch. TSC-28.

EXCEPTION 5: SFAS 106 (R.D. 45 to 50)

At pages 45 to 50 of the Recommended Decision, the ALJ discusses the Company's claim for costs related to SFAS 106. As the ALJ notes, the Company proposes to recover a total of approximately \$28 million. This includes approximately \$26 million in current costs plus \$1.8 million for the recovery of deferred SFAS 106 costs. The claim for deferred SFAS 106 costs represents a 17.3 year amortization of the approximately \$31 million of incremental costs incurred under SFAS 106 from the date it became effective on January 1, 1993 until the end of the future test year. R.D. at 45. The OCA, and other parties, proposed a disallowance of the \$1.8 million annual amortization of the deferred SFAS 106 costs based on the Commonwealth Court's holding in Popowsky v. Pennsylvania Public Utility Commission, 164 Pa. Commw. 338,

642 A.2d 648 (1994)(PP&L 1994). The ALJ rejected these proposed adjustments and allowed the Company recovery of these deferred costs. The OCA excepts to the ALJ's recommendation.

As noted above, the deferred costs at issue in this proceeding represent the incremental costs under SFAS 106 from January 1, 1993 until the end of the future test year. In December 1992, PP&L filed a Petition with the Commission seeking permission to defer these costs for accounting purposes, and to recover these costs in future rates. The PUC approved the Petition (Pa. P.U.C. v. PP&L, Docket No. P-00920635 (Entered May 6, 1993)). The PUC's Order was subsequently reversed by the Commonwealth Court wherein the Commonwealth Court concluded that "the incremental costs would be prohibited by the rule against retroactive ratemaking and the PUC's order improperly assures future recovery." Popowsky v. Pennsylvania Public Utility Commission, 164 Pa. Commw. 338, 345, 642 A.2d 648, 651 (1994).

Despite the Commonwealth Court ruling in PP&L 1994, the ALJ ruled that the costs were recoverable, finding that the SFAS 106 change was an extraordinary event which should be recognized. R.D. at 50. The ALJ also found that the case law could be read either way. Id. The OCA submits, however, that the case law is clear that these costs are prohibited from recovery in a base rate case by the law of this case and the rule against retroactive ratemaking. The costs which the ALJ would allow in this case are the very costs which the Commonwealth Court held could not be recovered in a future rate case. PP&L 1994, supra. Indeed, this was the whole point of the OCA's appeal in the PP&L case.

The Commonwealth Court specifically addressed the issue of whether the costs at issue were "extraordinary" costs deserving of an exception to the rule against retroactive ratemaking. The following excerpts from the Court's opinion are directly on point:

Extraordinary expenses are often described as unanticipated and non-recurring. . . . 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 the test years meaningless. . . .

These principles, though not explicitly, were applied in PECO. The costs of the pollution control devices in PECO were not extraordinary because those costs would be recurring as part of the cost of maintaining the existing facility. Also, the utility could have recovered the costs in rates had it filed its rate case earlier. Similarly, in this case, the incremental costs in 1993 are recurring; PP&L will be continually incurring those costs because it was required to change to the accrual method. Also, PP&L could have recovered those costs had it filed a rate case rather than a request for declaratory order.

* * *

Because the incremental costs were, in fact, anticipated before the request for declaratory order was filed and because the costs are recurring and could otherwise be recoverable in rates, the exception for "extraordinary" expenses does not apply.

PP&L 1994, 164 Pa. Commw. at 346-347, 642 A.2d at 652-653.

Most importantly, the Commonwealth Court considered the question of whether recovery of these costs would be improper in future rates. The Court stated:

Because the incremental costs recovered in some future rate case would relate to 1993 and the years up until the next rate case, what PP&L requested and the PUC awarded is retroactive ratemaking.

PP&L 1994, 164 Pa. Commw. at 346, 642 A.2d at 652. The Court went on to explain:

[W]e believe that requiring future ratepayers to pay not only the transitional obligation costs of changing to the accrual method but also the incremental costs incurred in 1993 and beyond until the next rate case unfairly burdens ratepayers.

Id.

The OCA submits that it is clear from the Commonwealth Court Order that recovery of these costs by PP&L is barred by the prohibition against retroactive ratemaking. In a similar

case involving West Penn, the Commission denied West Penn Power Company's claim for its prior period SFAS 106 costs on the grounds that the claim was untimely and was precluded by the rule against retroactive ratemaking. Pa. P.U.C. v. West Penn Power Company, Docket No. R-00942986, slip op. at 30-35 (Order entered December 28, 1994) (West Penn 1994). In addition, the Commission found in West Penn that these costs were not extraordinary and do not qualify for an exception to the rule against retroactive ratemaking. Id. at 31.

The OCA submits that based on the Commonwealth Court's holding in PP&L 1994, the Commission must deny PP&L recovery of its deferred SFAS 106 costs. For the reasons set forth above, and for the reasons set forth in the OCA's M.B. at 151-155 and R.B. at 67-71, the ALJ's recommendation should be rejected. Accordingly, the Company's net income should be adjusted by \$900,000 on a Pennsylvania jurisdictional basis as shown on Schedule TSC-11.

EXCEPTION 6: Discount Rate (R.D. 53 to 55)

The OCA recommended in its Main Brief that PP&L's proposed 7.5% discount rate for its pension and postretirement benefit expenses should be rejected and that a rate of 8.5% should be utilized. OCA M.B. at 147-151. The OCA proposed this adjustment because the Company failed to provide sufficient evidence to support the discount rate it selected, and record evidence revealed that PP&L's discount rate was unreasonably low and would overstate expense. The ALJ did not adopt the OCA's recommended discount rate of 8.5%. The ALJ, although he commented upon the quality of PP&L's defense of its proposed rate, accepted PP&L's proposed 7.5%. R.D. at 54. The OCA excepts to this aspect of the ALJ's decision.

It is the OCA's position that PP&L failed to provide sufficient evidence to support its proposed 7.5% discount rate. OCA M.B. at 147-151. PP&L's witness testified on cross-

examination that the discount rate is normally based on investment grade bonds and it is intended to reflect the time value of money. Tr. 88. However, the Company's witness offered no explanation of how the Company selected its proposed rate. The Company stated that its proposed rate "was determined based on a detailed analysis of a variety of factors." PP&L M.B. at 90. Yet, the Company failed to enumerate or discuss these factors.

As explained in the OCA's Main Brief, the Company selected a discount rate of 7% for 1994. OCA M.B. at 148. The 1994 rate was selected after considering the yields on four different types of investment grade bonds as of December 31, 1993. Id. An analysis of the yields on these bonds as of December 1994, however, shows that the yield on each type had increased by approximately 1.5%. Id. Thus, OCA witness Catlin concluded that this data supported an increase in the discount rate of more than the .5% proposed by PP&L. The OCA's recommended 8.5% rate corresponds with the approximate 1.5% increase in bond yields as of December 1994. See, OCA M.B. at 149-150. In addition, the reasonableness of the OCA's recommended discount rate is supported by the fact that PP&L's own actuary, and other actuaries, have recommended discount rates in the rate of 8.5% for 1995 for other utilities. See, OCA M.B. at 149-150. For example, PP&L's actuary, Towers Perrin, recommended an 8.75% discount rate to Pennsylvania- American Water company ("PAWC") for 1995. Tr. 91-92. PP&L has failed to differentiate its case from those companies that have utilized a rate in the range of 8.5%.

The ALJ cites to the Company's arguments on page 32 of the Company's Reply Brief as the basis for his decision. R.D. at 54. However, these arguments were presented in PP&L's Main Brief and addressed in the OCA's Reply Brief at pages 64-67. To state that the

Company's proposed rate is consistent with the guidelines of SFAS 87 and SFAS 106, which "state that discount rates shall be determined so as to reflect the rates at which the pension benefits could be effectively settled" (PP&L R.B. at 32) is circular and not evidence that the Company's rate is appropriate.

Other than the Company witness Beers' conclusory assertion that, "PP&L's pension obligations likely can be settled at rates 25 to 50 basis points below long-term government yields" (PP&L M.B. at 32), PP&L has put no evidence on record to support its proposed discount rate of 7.5%. Furthermore, PP&L has put no evidence on record to support its proposed discount rate of 7.5%, and PP&L witness Beers has failed explain the reasonableness of his opinion. PP&L must demonstrate that its proposed discount rate is reasonable. PP&L R.B. at 32. The OCA submits that it has not done so and that the OCA has established a record that supports its recommended 8.5% discount rate. As the ALJ stated, the OCA has provided a "substantial case" concerning this issue that is "persuasive". R.D. at 54. For these reasons, the OCA submits that its adjustments should be adopted as shown on Sch. TSC-9 and Sch. TSC-10.

EXCEPTION 7: SFAS 112 (R.D. 55 to 56)

The OCA excepts to the ALJ's rejection of the OCA's SFAS 112 adjustment that disallows an accrual in the future test year for the projected increase in the future liability of the Company for long term disability and survivor income benefits. R.D. at 55-56. The ALJ found that "this item [of expense] should be treated like other similar items" (presumably other benefit expenses such as under SFAS 106) and recommended the accrual be included in rates. Id. The OCA submits that there is simply no point in switching to an accrual basis if the Company plans

to pay for these benefit costs on a pay-as-you-go basis, as the Company has admitted that it does. See, OCA M.B. at 156-157. The ALJ's recommendation fails to consider that the Company has stated that it will not establish a separate fund for this liability if it recovers these costs prior to incurring them. Id. As OCA witness Catlin stated, "Test year expenses already include the annual cost associated with paying post-employment benefits. Ratepayers should not be required to pay for future liabilities which PP&L itself does not intend to pay until they become due." Id. The OCA submits that the Company's proposed treatment is an unfair burden on ratepayers.

In addition, the reasons supporting the use of the accrual method for ratemaking purposes for other benefit expenses under SFAS 106 are not present for the potential liability under SFAS 112. SFAS 112 does not create a significant, long-term difference between cash and accrual expenses for which FASB has determined a regulatory asset will not be allowed. OCA M.B. at 157. Therefore, the expenses under SFAS 112 and SFAS 106 should not be treated the same for ratemaking purposes. The OCA submits that it is unfair to burden ratepayers simply to maintain consistent treatment of benefit expenses, particularly absent any evidence that the Company is required, or intends, to place these funds in a dedicated trust. For these reasons, the OCA submits that the Company's SFAS 112 accrual should be disallowed.

EXCEPTION 8: Susquehanna Early Window (R.D. 56 to 62)

At pages 56 to 62, the ALJ addresses the Company's claim to recover its deferred "early window" costs associated with Susquehanna Units 1 and 2. These deferred costs are associated with operating and maintenance expenses incurred between the time when the units entered commercial operation and when they were recognized in rates. These costs were incurred by

the Company in 1983 for Susquehanna 1 and in 1985 for Susquehanna 2. R.D. at 57. The ALJ disallowed the Company's claim for recovery of its early window costs associated with Susquehanna 1, but allowed the Company the recovery of its deferred costs associated with Susquehanna 2. The OCA excepts to the ALJ's decision to permit the Company recovery of its deferred "early window" costs for Susquehanna 2.

The ALJ accepted PP&L's proposed amortization of its deferred early window costs for Susquehanna 2 finding that "the financial impact is significant and the utility should not be forced to time its rate case exactly, to meet the timing of the plants." R.D. at 61. In addition, the ALJ states he is inclined to allow the recognition because "the Commission had indicated to PP&L that, absent imprudence or some other similar problem, it could recover these costs later." R.D. at 61.

Initially, the OCA would note that it disagrees with the ALJ's reading of the Commission's Declaratory Orders regarding the accounting treatment for these deferred costs. When the Commission granted PP&L's petitions for permission to defer the Susquehanna early window costs for accounting purposes, it specifically stated in each case that the issuance of the Order was not a determination that the Company may recover the deferred costs. In the Susquehanna 1 Order the Commission explicitly stated:

The burden to show the justness and reasonableness of any proposed rate change, including recovery of deferred costs shall remain squarely with PP&L. In the appropriate rate case, we fully retain and will vigorously exercise our statutory duty to review all costs associated with Unit 1, including the deferred debit and credit accounts, and determine the reasonableness and propriety thereof prior to authorizing any change in rates.

Petition of Pennsylvania Power & Light Co. for Declaratory Order, Docket No. P-820367
(Order entered July 29, 1982). The Commission, in considering PP&L's request that the

Commission grant approval of rate recovery, continued to clarify its ruling:

For the identical reasons stated above, we deny the Petition to the extent that PP&L requests approval to amortize any deferred costs over a five year period. This issue is clearly substantive in nature and an approval of this claim now would be dispositive of the issue in the rate case and prejudicial to the parties' due process rights. The parties may address the propriety of recovery, the proper amortization and reasonableness of any deferred costs in the Company's rate case which seeks recognition thereof.

Id.

In its Petition regarding "early window" treatment for Susquehanna 2, PP&L sought, and the Commission granted, relief that was identical to that granted in the Commission's Order regarding Unit 1. Petition of Pennsylvania Power & Light Co. for Declaratory Order, P-830461 (Order entered November 9, 1983) In its ordering paragraph 3 of that Order, the Commission explicitly stated:

The issuance of this Order does not in any manner whatsoever determine the used and useful nature of Susquehanna Unit 2. Also, it is not a determination by the Commission that the costs involved were prudently incurred, that the energy savings were properly recorded or that the Company may recover deferred costs or retain deferred energy savings. Any claim for recovery of these costs will be subject to subsequent Commission audit and final disposition in an appropriate proceeding filed subsequent to the entry of a Final Order in the Susquehanna 2 rate case proceeding. . . . The question of whether the Company may recover the deferred costs, the reasonableness of these costs, and the merits of a cost recovery mechanism will be determined by the Commission in said subsequent proceeding.

Id.

As can be seen from the above language in the Commission's Orders, the Commission never indicated to PP&L that, absent imprudence, these costs would be later recovered. Additionally, the Commission, in numerous cases where it has considered a utility's request for recovery of deferred costs, has made clear that actual recovery of deferred costs is not to

become a part of routine regulatory practice. Rather, the Commission has cautioned that each request must be considered to determine if an exception to the rule against retroactive ratemaking is warranted.¹¹ Re Pennsylvania Power Co., 59 Pa. PUC 541, 545 (1985). See also, Pa. P.U.C. v. Philadelphia Electric Co., 74 Pa. PUC 1, 235 (1990) (PECO 1990)(concurring opinion of Commissioner David W. Rolka).

The Commission has granted limited exceptions to the rule against retroactive ratemaking to allow recovery of deferred early window costs. See, PECO 1990 and Pa. P.U.C. v. Pennsylvania Gas & Water Co., 79 Pa. PUC 349 (1993). In cases considering this issue, the Commission has established a three pronged test that requires the utilities to show the following:

- (1) The request is timely:
- (2) The costs are both extraordinary and nonrecurring; and
- (3) The denial of recovery would have a substantial negative financial impact on the utility.

PECO 1990, 74 Pa. PUC at 111; PG&W 1993, 79 Pa. PUC at 369; and Pa. PUC v. Pennsylvania American Water Co., Docket No. R-932670, slip op. at 71 (July 26, 1994)(PAWC 1994).

In considering claims for recovery of "early window" deferred costs, the Commission

¹¹ The OCA submits that the fundamental principles against retroactive ratemaking, affirmed by the Courts in a long line of cases, requires that PP&L's early window claim for both units be rejected as a matter of law. See e.g., Cheltenham & Abington Sewerage Co. v. Pennsylvania Public Utility Commission, 344 Pa. 366, 25 A.2d 334 (1942); Barasch v. Pennsylvania Public Utility Commission, 507 496, 491 A.2d 94 (1985); Philadelphia Electric Co. v. Pennsylvania Public Utility Commission, 93 Pa. Commw. 410, 502 A.2d 722 (1985); and Popowsky v. Pennsylvania Public Utility Commission, 164 Pa. Commw. 338, 642 A.2d 648 (1994). Since the ALJ analyzed PP&L's claim as to whether it warranted an exception to the rule against retroactive ratemaking, the OCA will focus its exception on that point.

has clarified the evidence that must be adduced to demonstrate that recovery is reasonable and appropriate. In his concurring opinion in PECO 1990, Commissioner Rolka explained:

While the PUC relies on a test year concept for setting rates, it is well known that the ultimate level of rates authorized are designed to recover prospective costs of operations, due to their fluidness, will probably differ in many respects from the Company's test year predictions. Hence the general rule against line-by-line examination of the accuracy of a utility's predictions of revenues and expenses is well taken.

To reconcile this basic regulatory maxim in the analysis of this issue, I submit that, in future cases in which a window claim is presented, evidence should be adduced as the Company's financial operations as a whole for the period in which the window costs were experienced. This evidence should reveal the true financial impact of the lack of recovery of the window costs.

PECO 1990, 74 Pa. PUC at 235. Commissioner Rolka further clarified that in examining the financial impact on the utility, it is important to consider the past periods. Commissioner Rolka stated:

The question of whether the window costs are extraordinary should be answered by examining the utility's financial operations during the period that the costs were experienced and determining whether the lack of recovery of those costs had a deleterious effect on the utility. . . . [To] be truly extraordinary, it must be demonstrated, based on all the other financial transactions experienced during the same period, the Company was not compensated for these costs.

Id.¹²

The OCA submits that the ALJ correctly found that PP&L's claim for recovery of Susquehanna 1 "early window" costs could not meet the standards set forth by the Commission that would justify recovery. The OCA submits, however, that neither does the Company's claim for recovery of "early window" costs for Susquehanna 2.

¹² In PAWC 1994, the Commission applied the test as set forth in PECO 1990 and ruled against the Company's proposal to recover "window" costs.

Notably, the Company has waited over nine years to file for recovery of the Susquehanna 2 early window costs. During this time period, PP&L had no constraints on its ability to seek rate relief, and voluntarily elected not to file for rate relief. As OCA witness Catlin explained:

During that time period, PP&L voluntarily elected not to file for rate relief, presumably because it believed its earnings were at or above what the Commission would deem to be a reasonable level. Unless PP&L can establish that it was not earning a reasonable return and would not have earned a reasonable return had it amortized the early window costs during the last ten years, it should not now be allowed to recover the early window deferrals.

OCA St. 6 at 28.

Moreover, the OCA submits that the Company has not demonstrated that the denial of recovery of its early window costs would have a substantial negative impact. Company witness Bernini quantified the impact of a write-off, if recovery for both units was denied, as amounting to 25¢ per share, as compared to 1994 earnings of \$1.41 per share. PP&L St. 3-R at 13. This one-time, one-year reduction amounts to approximately 17.7%. Id. Had the write-off occurred in 1985 when the costs were incurred, the one-time, one-year reduction in the Company's earnings would have been approximately 20% (53¢/share as compared to 1985 earnings of \$2.68/share). PP&L St. 3R at 14.

The OCA submits that the Company has not demonstrated that the impact of a write-off associated with these costs is "significant." In the two cases where the Commission has allowed recovery of such costs, the write-offs would have reduced earnings by 50%. PECO 1990, 74 PA. PUC at 110; PG&W 1993, 79 PA. PUC at 366. The OCA submits that PP&L's claim does not approach the level of loss which the Commission found justifies an exception to the rule

against retroactive ratemaking.¹³

For the reasons set forth above, and for the reasons set forth in the OCA's M.B. at 103-117, and R.B. at 48-52, the OCA submits that the Company's claim for recovery of Susquehanna 2 early window costs should also be denied. The OCA submits that current ratepayers should not be asked to bear these past costs as such constitutes improper retroactive ratemaking. Moreover, the OCA submits that PP&L has not established that its claim in this case is justified as a limited exception to the rule against retroactive ratemaking. As such, the OCA submits that the Company's expense claim should be further reduced by \$1,886,000 to reflect the additional disallowance of the amortization of the Susquehanna 2 early window costs.

EXCEPTION 9: Susquehanna Refueling Outage Expense (R.D. at 63).

PP&L normalizes refueling outage costs by amortizing the costs of the outage over the period between refueling outages, which is typically around 18 months. The OCA submits that the ALJ erred in accepting PP&L's determination of future test year refueling outage expense, which was based on the completion of the amortization of Reload Outage 7 and the initiation of Reload Outage 8 at Susquehanna Unit 1 and the amortization of Reload Outage 6 at Unit 2. R.D. at 63. As discussed in the OCA's Main and Reply Briefs, due to the unusually high level of expense associated with Reload Outage 6 at Unit 2, OCA witness Catlin adjusted the amortization of refueling outage costs to reflect the annualized level of costs based on the most

¹³ Additionally, in Pa. P.U.C. v. PECO, 58 Pa. PUC 7 (1983), the Commission considered the magnitude of the deferred expenses in relation to the overall rate base claim of the Company. In that case, the Commission found that the size of the deferral (\$41,447,000) in relation to the overall rate base claim of the company (\$2.8 billion), or about 1.5%, "is not such as to severely impact the Company's financial condition." Id. at 44. In the case at bar, the size of the deferral (\$39 million) in relation to the overall rate base (\$5.0 billion) is about 0.77%.

recent outage for each unit as of the end of the test period.¹⁴ OCA M.B. at 117-122; OCA R.B. at 52-54.

The OCA submits that the ALJ's finding that the costs for Reload 6 at Unit 2 were not "so out of line that it should not be used as an appropriate measure for this ratemaking calculation" fails to consider the many problems that occurred during Reload 6. R.D. at 63. As discussed in the OCA Main and Reply Briefs, the evidence provided by the Company establishes that PP&L experienced problems during Reload 6 at Susquehanna Unit 2 which resulted in higher costs. OCA M.B. at 118-121; OCA R.B. at 52-54. PP&L witness Berish testified that Reload 6 lasted 18 days longer than planned and that there were problems during Reload 6, including four accidents involving the breaking of refueling masts, and a problem with a jet pump beam which required an unplanned replacement. Tr. 2016-2017. The Company presented no evidence that the costs associated with correcting these problems are typical or recurring costs. Accordingly, the ALJ's determination to utilize the costs associated with Reload 6 at Unit 2 to determine PP&L's refueling outage expense should be rejected.

As discussed above and in the OCA's Main Brief at 117-122 and Reply Brief at 52-54, the OCA submits that due to the problems that occurred during Reload 6 at Unit 2, the costs associated with that outage were atypical and these higher costs should not be included in determining the proper level of refueling outage expense. Adoption of the OCA's adjustment reduces total company expenses by \$1,416,000 and jurisdictional expenses by \$1,111,000. The resulting increases in net income are \$819,000 and \$643,000, respectively. OCA St. 6, Sch.

¹⁴ Mr. Catlin based his adjustment on the costs of Reload 8 at Susquehanna Unit 1, which was scheduled to take place from March 25 through May 22, 1995, and Reload 7 at Unit 2, which is scheduled to take place from September 16 to November 13, 1995. OCA St. 6 at 30

TSC-18.

Exception 10: Social Programs (R.D. at 80).

In his Recommended Decision, the ALJ recommended no adjustments to PP&L's request for Commission approval to implement eight social programs¹⁵ and its claim for \$3,530,000 in test year expense to fund the energy-related portions of these programs. R.D. at 80. The OCA had proposed that due to the preliminary nature of the Company's proposal, the Commission should require the Company to provide the final implementation plans and a detailed outline of the future reporting requirements on the expenditures of these programs with its compliance filing in this rate proceeding.¹⁶ OCA M.B. at 160-162; OCA R.B. at 74-75. This request was not addressed in the Recommended Decision.

In approving PP&L's claim, the ALJ recognized a "need for scrutiny" of PP&L's social program initiatives. R.D. at 80. However, absent detailed information relating to the implementation, expenditures, and results of these programs, it will be difficult for the Commission to evaluate the effectiveness of these programs in benefitting ratepayers through the energy efficiency initiatives. The OCA submits that should the Commission adopt the ALJ's recommendation to allow PP&L to fund the social programs in this rate proceeding, the Commission should require PP&L to provide the final implementation plans and a detailed outline of the future reporting requirements with its compliance filing in this rate proceeding.

¹⁵ The Programs are: Build-A-Neighborhood; Affordable Housing; Small Business Program; Keep Warm Plan; Payment Protection Plan; Winter Emergency Plan; Operation HELP Contribution Enhancement Plan; and CARES Extension Pilot Program. PP&L St. 11 at 13-31.

¹⁶ The Company has already agreed to "submit quarterly reports to the Commission and the OCA on the implementation status and expenditures of these programs." PP&L St. 11R at 14.

Nuclear Decommissioning Costs (R.D. at 96-100)

EXCEPTION 11: Non-Radiological Decommissioning Costs

In this proceeding, PP&L's nuclear decommissioning expense claim is based on an \$804 million (1993 \$) estimate for costs related to the decommissioning of the two nuclear units at Susquehanna Steam Electric Station ("SSES") beginning in the year 2022. PP&L's claimed annual decommissioning expense is \$30.042 million on a total Company basis, \$23.570 million on a Pennsylvania jurisdictional basis. As discussed in the OCA's Main and Reply Briefs, the OCA proposed the removal of \$127.4 million in non-radiological decommissioning costs from the Company's \$804.3 million decommissioning estimate. OCA M.B. at 176-188; OCA R.B. at 77-81.

The OCA submits that the cost of non-radiological decommissioning should not be included in rates at this time. Unlike radiological decommissioning, there are no federal or state regulations requiring the decommissioning of non-radiological structures. In addition, the public safety concerns associated with non-radiological structures do not rise to the same level as those for radiologically contaminated areas, particularly since PP&L presented no evidence that it intends to abandon the SSES site. OCA M.B. at 176-188. However, the ALJ found that the limited nuclear exception to Penn Sheraton Hotel et al. v. Pa. P.U.C., 198 Pa. Super. 618, 623-627; 184 A.2d 324, 327-329 (1962) ("Penn Sheraton") is applicable and allowed for the recovery of non-radiological decommissioning costs.¹⁷ R.D. at 98. The OCA excepts to the

¹⁷ In 1978, the Commission granted a limited exception to the Penn Sheraton prohibition to allow for recovery of costs associated with radiological decommissioning. See Pa. P.U.C. v. Pennsylvania Electric Company, 51 Pa. PUC 649, 669 (1978); Pa. P.U.C. v. Philadelphia Electric Company, 55 Pa. PUC 78, 95 (1981). Nine years later, in Pa. P.U.C. v. Pennsylvania (continued...)

ALJ's determination.

As discussed in the OCA's Main and Reply Briefs, the OCA submits that in view of the recent Commonwealth Edison¹⁸ decision, and the recent proposed changes in NRC regulations, as well as an examination of the facilities and equipment included in the non-radiological decommissioning estimate, the Commission should re-evaluate its recent practice of including non-radiological decommissioning costs in the decommissioning estimate.

The OCA is only requesting that the costs related solely to non-radiological decommissioning be removed from the decommissioning cost estimate. OCA M.B. at 181-188. Those costs associated with non-radiological structures that will be impacted by the removal of radiological structures are already included in the radiological estimate as "cascading" costs. OCA M.B. at 180-182. The ALJ's determination failed to consider that the SSES site will still be a viable site for future electric generation use, after radiological decommissioning is

¹⁷(...continued)

Power Company, 64 Pa. PUC 308 (1988) ("Penn Power"), the Commission allowed recovery of non-radiological decommissioning costs because of safety concerns related to damage to non-contaminated facilities during the removal of contaminated facilities. See also, Pa. P.U. C. v. Duquesne Light Company, 66 Pa. PUC 518, 679-680 (1988); Pa. P.U.C. v. Pennsylvania Power Company, 67 Pa. PUC 91, 139-140 (1988).

¹⁸ In Re Commonwealth Edison, 158 PUR4th 458, 499 (Illinois Commerce Commission 1995), the Illinois Commerce Commission denied Commonwealth Edison Company's request for non-radiological decommissioning costs finding that:

The burden is on the Company to prove that it will not re-use old structures. The Company has failed to convince the Commission that nonradioactive structures will not be used in the future. The Commission cannot allow ratepayers to pay for returning facilities to greenfield status when, in fact, some facilities may be re-used.

Id. 158 PUR4th at 499.

complete. Accordingly, the OCA submits that PP&L's decommissioning cost estimate should continue to be based solely on radiological decommissioning costs. Removal of the non-radiological costs from PP&L's decommissioning claim results in a reduction of \$3,195,000 on a total Company basis and by \$2,506,000 on a Pennsylvania jurisdictional basis.¹⁹

EXCEPTION 12: Nuclear Decommissioning Trust Fund Earnings Rate. (R.D. at 99-100).

PP&L places the decommissioning funds collected from ratepayers into an external Nuclear Decommissioning Trust Fund. This Fund produces earnings which are then incorporated into the fund. In its claim, PP&L assumes a net of tax rate of return averaging only 5.5% over the period from 1995 until completion of decommissioning for the earnings of this Fund. The OCA submits that PP&L's estimate of trust fund earnings is too low, particularly in light of PP&L's request to utilize a prudent person standard for fund investment as a result of a change in federal law. The OCA submits that the earnings estimate should be increased to 7.5%. OCA M.B. at 169-176; OCA R.B. at 85-86.

The ALJ adopted PP&L's 5.5% earnings estimate, despite recognizing that it was a "conservative" estimate. R.D. at 99. The OCA submits that the ALJ erred in not adopting a higher earnings estimate especially since he also granted PP&L's request to remove the "black lung" restrictions on investments. Allowing PP&L to understate the return on the Trust Fund results in a significant increase in the decommissioning revenue requirements which PP&L is seeking from its ratepayers in this case. OCA M.B. at 169-176.

¹⁹ The OCA submits that should the Commission adopt the ALJ's recommendation to include non-radiological costs in PP&L's decommissioning claim, that the Commission must also remove the contingency associated with these non-radiological costs. The OTS recommendation on contingencies reflects the removal of the contingency component from both radiological and non-radiological cost estimates. OTS M.B. at 46-53.

OCA witness Kahal, after analyzing PP&L's investment strategy and reviewing market conditions, recommended increasing PP&L's 5.5% after tax earnings rate to a 7.5% after tax earnings rate. The Company did not present any evidence that Mr. Kahal's 7.5% was inconsistent with current and projected market conditions. *Id.* at 174. The OCA submits that the adoption of the 5.5% recommendation is unreasonably low in light of PP&L witness Hill's testimony that if the restrictions are removed, "[T]he Company anticipates that a broader investment strategy would produce higher returns than are now realized under the current investment requirements." *Id.* at 170.

Accordingly, for the reasons set forth above, and for the reasons set forth in the OCA's M.B. at 169-175, and R.B. at 84-86, the OCA submits that the ALJ's recommendation should be rejected and the Company should be required to increase its rate of return on its decommissioning trust fund earning from 5.5% to 7.5%.

EXCEPTION 13: Susquehanna Depreciation (R.D. 109 to 115)

At pages 109-115 of his Recommended Decision, the ALJ discusses the Company's proposal to change the depreciation methodology for pre-1989 Susquehanna plant from the modified sinking fund approach to a straight-line method. The Company's proposal increases the Company's claimed depreciation expense by \$22,864,760 on a Pennsylvania jurisdictional basis. OCA St. 5 at 7. The ALJ recommends that PP&L be permitted to move to the straight-line method early finding no particular reason to require PP&L to continue the modified sinking fund method. R.D. at 114-115. The OCA submits that the ALJ erred in adopting this claim. The Company has failed to justify its proposed change in methodology that will increase expense by over \$22.8 million.

As the OCA set forth fully in its Main Brief at pages 122-129, and its Reply Brief at 54-57, the Company's proposal to change from the modified sinking fund method to a straight-line method is flawed in that it distorts the relationship between depreciation accruals and rate base, and results in the Company overrecovering from ratepayers. As explained by OCA witness Johnson:

The major objection I have to the Company's proposal is that it only levelizes one aspect of capital recovery--the depreciation accrual--and does not levelize the other aspect of capital recovery--return on capital invested.

In normal ratemaking practice, there is a connection between depreciation accruals and rate base through the mechanism of providing a return on rate base (i.e., on adjusted net plant), which is gross plant less accumulated depreciation. The greater the accumulated depreciation over time, the lower the rate base and its return. This relationship is time dependent. . .[E]very time a rate case is filed, the amount of test year rate base is dependent on the depreciation accrued up to that time. A significant change in the size of the depreciation accrual would distort that relationship, at least for a period of time after the change.

OCA St. 5 at 5-6. Thus, what PP&L has proposed is that its depreciation accrual be levelized at a higher rate, but it has failed to recognize the reduced return requirements on its rate base that will result from this accelerated depreciation.

As OCA witness Johnson noted, this reduced return requirement can be significant, ranging from \$19 million to \$54 million per year. OCA St. 5A at 5. In contrast, if the Company remained with the modified sinking fund approach, the recovery of capital would be fairly constant. Dr. Johnson explained:

The increase in annual depreciation accrual from one year to the next never exceeds \$20 million. Moreover, because net plant is declining each year, this \$20 million is largely offset by reduction in return on investment that is required.

Note that the total recovery of capital would be relatively constant under the modified sinking fund. The increase in the depreciation accruals is almost exactly

offset by the decrease in return on rate base. That is exactly what the MSF is calculated to do.

OCA St. 5 at 4-5. The OCA submits that the continuation of the MSF method represents a fair balance of ratepayer and shareholder interests. The Company has not justified its levelization proposal that would increase depreciation expense by \$22.8 million, and result in an overrecovery from ratepayers.

For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at pages 122-129, and its Reply Brief at 54-57, the OCA submits that the Company's proposal to change its depreciation method for pre-1989 Susquehanna plant from a modified sinking fund method to a levelization method should be rejected.

EXCEPTION 14: Consolidated Tax Savings (R.D. at 134-136).

The OCA submits that the ALJ erred in finding that there was no basis for a consolidated tax adjustment in this proceeding. R.D. at 134-136. In particular, the OCA excepts to the ALJ's conclusion that the OCA's adjustment is an attempt to impute "past tax losses" related to PP&L's mining operations to future rates for PP&L. Id. at 136. The OCA excepts to this recommendation since it fails to recognize that the OCA's consolidated tax savings adjustment relies on the future test year projections provided by PP&L. OCA M.B. at 200-203; OCA R.B. at 91.

In this proceeding, consistent with Commission precedent, OCA witness Catlin calculated the consolidated tax savings allocable to the Company utilizing what has become known as the modified effective tax rate method. OCA M.B. at 198-200. In calculating this adjustment, Mr.

Catlin relied on the most recent data provided by the Company.²⁰ OCA M.B. at 200-203; OCA R.B. at 89-91. The ALJ's finding that there is "no basis for projecting the general situation of the past into the future" ignores the evidence that in this proceeding, PP&L projected losses for the future test year of over \$5.75 million. OCA M.B. at 202, OCA St. 6A at 12. Despite the OCA's request for additional data, the Company presented no evidence to support its position that these losses will not continue into the future. OCA M.B. at 202-203; OCA R.B. at 90. Thus, it is appropriate to include these future test year losses in the consolidated tax calculation.

In addition, the OCA submits that the ALJ erred in his acceptance of the "ECR argument of PP&L." R.D. at 135. As, set forth in the OCA's Main and Reply Briefs, PP&L failed to provide any evidence to support its claim that tax savings have already been passed through to customers through the ECR. OCA M.B. at 203; OCA R.B. at 90-91. The OCA submits that PP&L retains the burden of proof to establish each element of its claim. See OCA M.B. at 3-6. Thus, the ALJ's recommendation to reject the OCA's consolidated tax savings adjustment should be rejected. Consistent with well-established Pennsylvania precedent, PP&L should be required to pass on the tax savings associated with its consolidated tax filing. Adoption of this adjustment reduces federal income tax expense by \$2,548,000 on a total company basis and \$2,161,000 on a Pennsylvania jurisdictional basis. OCA St. 6, Sch. TSC-25; OCA M.B. at 198-203; OCA R.B. at 89-91.

²⁰ The data provided by PP&L demonstrated that the mining companies that produced the majority of the taxable losses had continued to generate tax losses in the years following their closing, including projected losses during the future test year. OCA St. 6A at 12 (emphasis added).

EXCEPTION 15: Capital Structure (R.D. at 159-160)

In this proceeding, PP&L's projected capital structure relies, in part, on a \$100 million equity issuance scheduled to take place in August 1995, prior to the issuance of the Commission's Final Order.²¹ As discussed in the OCA's Main and Reply Briefs, the OCA did not object to using the projected capital structure, as long as the Company updated the Commission on the status and amount of the planned equity infusion, and utilized only the actual amount of equity issued in the capital structure. However, if the equity infusion did not occur prior to the entry of the Commission's Final Order in this proceeding, the OCA recommended that PP&L's capital structure should be revised to exclude the projected equity infusion.

To date, PP&L has provided no additional information on the status of the equity issuance, even though PP&L's witnesses agreed that it would be reasonable to use the actual amount of equity issuance in the Company's capital structure. OCA M.B. at 213-214; OCA R.B. at 99. Absent firm evidence that the equity has been issued, PP&L should not be allowed to include it in its capital structure in this rate proceeding. See Pa. P.U.C. v. National Fuel Gas Distribution Corp., 73 Pa. PUC 552, 605-606 (1990). OCA M.B. at 213-215; OCA R.B. at 98-101.

Thus, the OCA excepts to the ALJ's finding that PP&L's projected capital structure is "reasonable," absent any evidence that the equity infusion in the amount projected by PP&L is proceeding as scheduled. R.D. at 159. The OCA submits that PP&L retains the burden to establish that the equity issuance has actually taken place prior to the entry of a final Order.

²¹ The \$100 million equity issuance which the Company indicated is scheduled for August 1995 increases PP&L's common equity ratio by nearly a full percentage point. PPLICA M.B. at 27.

Accordingly, the OCA submits that prior to the entry of a Final Order in this proceeding, PP&L should be required to update the Commission and the active parties of record on the status and amount of the planned equity infusion. Moreover, should the equity infusion not occur prior to the entry of the Commission's Final Order in this proceeding, PP&L's capital structure should be revised to exclude the projected equity infusion.

EXCEPTION 16: Accumulated Deferred Income Tax Associated With The Loss On Recquired Debt. (R.D. at 159-160).

In this proceeding the OCA recommended using the Company's actual capital structure with an adjustment to the cost of debt to reflect the accumulated deferred income taxes associated with the loss on reacquired debt (call premiums). OCA M.B. at 220-227; OCA R.B. at 101-104. In the alternative, if the Commission did not accept this adjustment, the OCA recommended that PP&L's rate base be adjusted to recognize the balance of accumulated deferred income taxes (ADIT) associated with the Company's loss on reacquired debt. OCA M.B. at 225-231; OCA R.B. at 102-103. The ALJ rejected the OCA's primary capital structure recommendation finding that Commission precedent allowed utilities to adjust their capital structures for the recovery of call premium expense. R.D. at 159-160. The OCA will not except to this recommendation. However, the ALJ also rejected the OCA's rate base adjustment associated with ADIT which must be adopted if the OCA's primary recommendation is rejected. Id. at 160. Thus, the OCA excepts to the rejection of its alternative adjustment.

The OCA submits that the ALJ's finding that it is reasonable to "match recovery of the cost of the premiums and the associated tax savings", in fact creates a mismatch. Id. As discussed in the OCA Main and Reply Briefs, the OCA's rate base adjustment recognized that the Company's practice of reacquiring debt gave rise to a tax timing difference, and hence,

deferred taxes. In other words, shareholders have already received the tax savings but ratepayers will only see the tax savings gradually over the next 10 to 15 years. OCA M.B. at 225-230. However, as OCA witness Catlin testified:

... nowhere in its calculations has PP&L recognized that it received an immediate tax benefit for the loss which served as a source of cost-free capital. Therefore, deducting the balance of ADIT on reacquired debt from rate base is necessary to recognize this balance as a source of non-investor supplied capital.

OCA St. 6 at 7. Moreover, as OCA witness Kahal explained: "[T]he issue with the deferred taxes is not whether the tax benefit dollars will be passed on to ratepayers but when. OCA St. 1B at 7. The OCA submits that the ALJ's recommendation fails to recognize that the rate base adjustment for the accumulated deferred income taxes associated with the loss on reacquired debt ensures that the Company only receives a return on the investor-financed portion of the asset, not on the portion financed by the taxing authority or ratepayers.²² Thus, the OCA submits that if the Commission adopts the ALJ's recommendation to allow PP&L to adjust its capital structure by the amount of the losses on reacquired debt, then the Commission must also adopt the OCA's adjustment to rate base in order to reflect the associated accumulated deferred income taxes. Absent this adjustment ratepayers will be denied timely recovery of the deferred taxes associated with PP&L's call premiums. As shown on OCA St. Sch. TSC-4, adoption of this adjustment reduces total Company rate base by \$47,863,000 and reduces Pennsylvania jurisdictional rate base by \$40,838,000.

²² PP&L witness Moul argued that since unamortized call premiums are not given rate base recognition, the OCA's adjustment should be rejected. However, as Mr. Kahal explained because Mr. Moul "subtracts the unamortized balance from debt balance for capital structure purposes he is in effect giving that balance a combined debt plus equity return, i.e., the dollar equivalent of putting it in rate base." OCA St. 1B at 8. OCA M.B. at 230.

EXCEPTION 17: Cost of Service Study (R.D. 189 to 205)

A. Peak and Average Methodology

At pages 189-205 of the Recommended Decision, the ALJ discusses the parties' alternative cost of service studies. The ALJ recommends adherence to PP&L's 12 CP method for allocation purposes. R.D. at 204-205. The ALJ rejects the OCA's proposed peak and average methodology for allocation of production plant based on his disagreement with the energy method of allocating production investment. R.D. at 205. In addition, the ALJ notes concern that the peak and average method does not explicitly address the energy element of production plant or the capacity involvement of energy costs. R.D. at 205. The OCA submits that the ALJ's concerns are misplaced. Indeed, the peak and average method is the only method presented on the record of this proceeding that recognizes how the energy requirements of the Company affect the Company's capacity planning decisions.

As set forth in the OCA's Main Brief, the 12 CP method utilized by PP&L for the allocation of production investment does not recognize that the cost of generating plant in service is partly determined by the amount of energy that the plant is expected to provide. OCA St. 3 at 5. Mr. Sipics, PP&L's witness on system planning issues, recognized the importance of serving the year round energy needs of its customers in capacity planning. As Mr. Sipics testified:

When you look at our base load units, the reason we spend a lot more capital than you would need to spend to build a combustion turbine is because we were looking to provide energy over greater periods of time.

Tr. 298. As OCA witness, Dr. Johnson further explained:

The energy requirements of the classes make up the total jurisdictional energy requirements of the Company, and the Company's energy requirements affect the

production investment decisions of the Company. If it were only necessary to meet the maximum demand (even the 12 monthly maximum demands) for a short duration, PP&L could do so at lowest cost by installing combustion turbine peaking units and would not need to install baseload generating capacity. In order to supply energy the year round and meet the maximum demands, the Company installs a mix of generation facilities--baseload, intermediate, and peaking.

OCA St. 3 at 8.

The OCA submits that the generation planning process must be reflected to the fullest extent possible in the cost of service study in order to make a determination of the reasonable relationship between cost incurrence and cost responsibility. As OCA witness Johnson explained:

The amount of investment in generating plants is a function of both the amount of capacity the utility has and the mix of its generating capacity. A utility with a high load factor could meet its total production costs at the lowest possible cost by having more baseload plant than a utility with a low load factor would have. Because the energy requirements of the utility are a factor in determining the amount of production investment, the energy requirements of the rate classes should be a consideration in allocating the production investment to the classes.

OCA St. 3 at 9. See also, CEPFOD St. 1 at 26.

The OCA submits that the peak and average methodology is the only methodology proposed in this proceeding that gives explicit recognition to both the amount of capacity required to meet the system peak demands and the energy demands of the class. The Commission has previously recognized the importance of recognizing these energy demands in classifying and allocating production investment. See, Pa. P.U.C. v. West Penn Power Co., 54 Pa. PUC 602, 634 (1981); Pa. P.U.C. v. Philadelphia Electric Co., 61 Pa. PUC 589, 678 (1986); and Pa. P.U.C. v. West Penn Power Co., 73 Pa. PUC 454, 518 (1990). In West Penn 1990, the Commission adopted the OCA's proposed peak and average method and stated:

We further agree with the ALJ that while each of the cost of service studies presented in this case may have some merit, the P&A study proposed by the OCA appears to be the most reasonable. We agree also with the ALJ's discussion in support of his recommendation to use the P&A method, particularly with his notation that the allocation of costs should reflect the Company's generating planning decisions with regard to base load capacity versus peaking capacity.

West Penn 1990, 73 Pa. PUC at 518. In accepting the ALJ's reasoning, the Commission quoted from the Recommended Decision as follows:

I agree with the OCA that the allocation of costs should reflect the Company's generation planning decisions with regard to base load capacity versus peaking capacity. This is done by including an energy allocation as well as a peak demand allocation in order to recognize the contribution of energy-intensive customers to the Company's capacity planning decisions. The P&A study accomplishes this task, while the single CP study fails to do so.

Id. at 516-517.

For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 266-277 and Reply Brief at 116-123, the OCA submits that the ALJ's recommendation to utilize a 12 CP method for allocation of production investment should be rejected. The OCA submits that the peak and average methodology should be utilized in that it best reflects the cost responsibility of the classes for the PP&L system. The peak and average method should be adopted as a reasonable and appropriate guide in determining revenue allocation in this proceeding.

B. Minimum System

At page 208, the ALJ adopts the Company's minimum system approach for separating costs into a customer component and a demand component. The OCA submits, however, that the Company's method overstates the amount of costs that are considered to be customer related, and should not be accepted for this reason. OCA St.3 at 14. The OCA presented an adjustment

to the Company's minimum system study to reduce this overstatement and reflected this adjustment in its cost of service study. OCA St. 3 at 14. The OCA submits that its adjustment, which corrects the overstatement of customer related costs, should be adopted in this proceeding.

The theoretical basis of the minimum system approach is that it is to represent entirely customer-related costs, i.e., costs that do not meet the engineering requirement for carrying the loads necessary for actual distribution. In implementing this approach in this case, the Company performed an analysis of each account required to construct a distribution system, and separated the investment in each account into a customer component by calculating the cost of a distribution system consisting of the smallest components currently being installed. OCA St. 3 at 14-15. The problem with this approach is that the transformer and conductor components that are being installed today can carry significant load. OCA St. 3 at 15. For example, the 10kVa overhead transformer utilized by PP&L in its study can easily carry 10 KW of demands. Id. See also, OCA St. 3B at 2-3.

Since these components have a load-carrying capability, they are not fully customer-related. The residual component is often considered to be demand-related. OCA St. 3 at 16. To correct for the resulting overstatement in customer-related costs, OCA witness Johnson proposed an adjustment that focused on the transformer investment since the constraining factor of the load carrying capability is the amount of transformer capacity. Dr. Johnson, for his adjustment, performed a calculation and developed an alternative demand allocator which accounts for the load carrying capability of the minimum system. OCA St. 3 at 17. This adjustment was incorporated into Dr. Johnson's cost of service study as shown on OCA St. 3, Exh. CEJ-1, Sch. 1. The effect of this adjustment on an individual basis is shown in OCA St.

3B, Exh. CEJ-4, Sch. 3.

The OCA submits that Dr. Johnson's adjustment to PP&L's minimum system study is reasonable, properly justified, and properly quantified. Dr. Johnson properly adjusted the demand allocator to account for the load carrying capability of the system so that the customer related component could be more accurately identified. For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 277-285, and its Reply Brief at 123-125, the OCA submits that the ALJ's recommendation to utilize PP&L's minimum system study should not be adopted. The OCA submits that its proposed adjustment to PP&L's minimum system study should be adopted by the Commission.

EXCEPTION 18: Revenue Distribution (R.D. 189 to 210)

The ALJ did not provide a specific revenue distribution, but appears to have adopted PP&L's proposed revenue distribution with some modifications. The OCA would note that the ALJ's acceptance of OCA's recommendations regarding the RTS rate class will result in a change to PP&L's proposed revenue allocation for the RTS class. Under the ALJ's recommendation, the percentage increase for the RTS class will be substantially the same as the percentage increase for the RS class.

To the extent that the ALJ has adopted the PP&L overall revenue distribution proposal, however, the OCA would except. The OCA submits that the OCA's proposed revenue allocation is reasonable and should be adopted in this proceeding. The OCA's proposed revenue allocation, under the Company's full rate increase request used for comparison purposes only, shows percentage increases of between 5.93% and 15.56%, with most increases around 11% to 11.7%, or near the system average. For the residential class, the OCA proposed that the

increase be no more than the system average increase. See, OCA M.B. at 291. The OCA proposed revenue distribution is fully supported by the OCA's cost of service study, and is consistent with the principles of rate continuity, consideration of customer impacts and gradualism. The OCA submits that its proposal is reasonable and should be adopted.

At page 227 of the R.D., the ALJ asks the parties to comment on the OSBA approach to a rate reduction or a small increase, which the ALJ recommends that the Commission adopt to the degree possible in such situations. The OCA supports a proportional scaleback, rather than the OSBA proposal.²³ The OSBA proposal, which appears to utilize a subtraction of a "constant differential," has the possibility of producing greater decreases, or even rate reductions for some classes, while other classes would experience greater increases in relation to the system average than those adopted by the ALJ. In other words, the process of subtraction under the OSBA method, rather than the multiplication under a proportional scaleback, may distort the relationship to the system average increase that was established. Thus, principles such as rate caps, or gradualism, may be distorted in the scaleback process. Moreover, the OSBA method contemplates the application of judgment after the rate relief is known, which is late in the process for the parties to review. For these reasons, the OCA submits that the effects of the OSBA's rate structure proposal are too uncertain to be adopted in this proceeding.

²³ Under a proportional scaleback, if the Company received one-half of its request, then each class' increase would be cut in half.

EXCEPTION 19: Residential Rate Design (R.D. 227 to 231)

A. Customer Charge

At pages 227-231, the ALJ addresses the issue of the proper level of the customer charge for rate classes RS and RTS. The Company had proposed an increase in the RS customer charge of 50%, from \$4.80 to \$7.20 per month. For RTS, the Company proposed an increase in the customer charge of 37%, from \$10.95 to \$15.00 per month. The ALJ recommended that both the RS and RTS customer charges be increased, but recommends a limitation of the increase for RS customers to a 35% increase. The ALJ also recommends that the customer charge increase be scaled back with lesser increases. R.D. at 230.

The ALJ accepts PP&L's cost of service analysis in support of the customer charge increases. In addition, the ALJ notes that his proposal is "something like the rate of inflation over the last ten years." R.D. at 230. The OCA submits, however, that the Company's cost of service study for customer charge contained costs that are not properly included in an analysis of the "basic customer cost" as defined by the Commission in a long series of cases. See, Pa. P.U.C. v. West Penn Power Co., 59 Pa. PUC 552, 612 (1985); Pa. P.U.C. v. West Penn Power Co., 73 Pa. PUC 454, 526-27 (1990); Pa. P.U.C. v. West Penn Power Co., 79 Pa. PUC 122, 218-220 (1993); Pa. P.U.C. v. Pennsylvania-American Water Co., Docket No. R-00932670, slip op. at 108-115 (Order entered July 26, 1994); and Pa. P.U.C. v. West Penn Power Co., Docket No. R-00942986, slip op. at 104 (Order entered December 29, 1994).

As the Commission has set forth in these cases, the customer charge should be designed to recover only those costs directly associated with metering and billing of residential customers. These costs include the costs for the meter and service drop, meter reading and billings. It

excludes consideration of the costs of transformation and distribution plant, administrative and general costs, uncollectibles, and other such costs. West Penn 1985, 59 Pa. PUC at 612; West Penn 1994, slip op. at 104.

In this case, the Company's determination of its customer costs included large amounts of allocated costs that are not included within the Commission's definition of "basic customer cost." As Dr. Johnson testified, the Company's calculation of customer cost includes:

[T]he return on meters, services, the portion of lines and transformers deemed by the Company to be customer-related, allocated portions of intangible plant, general plant and working capital; all allocated operating and maintenance expenses; depreciation expense on the above plant; and taxes.

OCA St. 3 at 23.

Even the Company's alternative calculation which excluded lines and transformers included large amounts of allocated O&M expenses, uncollectibles, administrative and general expense, and customer information and services. OCA St. 3 at 24. The OCA submits that these costs are not properly included in the determination of basic customer costs for determining customer charge. West Penn 1994, slip op. at 104.

OCA witness Johnson calculated the residential customer costs following the Commission's definition of "basic customer cost." Dr. Johnson determined that the basic customer cost for the RS class is \$4.73 monthly, which is below the current RS customer charge of \$4.80. OCA St. 3 at 24. For the RTS customer, Dr. Johnson determined a basic customer cost of \$8.29 monthly, which is below the current customer charge of \$10.95. OCA St. 3 at 25. Thus, the OCA submits that there is no cost justification for increasing the customer charge for either the RS or RTS customers at all, let alone by the 35% to 37% recommended by the

ALJ.²⁴

For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 305-308, and Reply Brief at 130-132, the OCA recommends that the customer charge for the RS and RTS classes be maintained at their current levels. Dr. Johnson's analysis demonstrates that these levels are sufficient to recover the costs of billing, metering, and services.

B. Energy Block Design

The ALJ also accepted the Company's proposal to increase the number of energy blocks for residential service from the current two blocks to three energy blocks. R.D. at 231. The Company's proposal uses a declining block structure, with the cents per kwh charge being reduced for each increasing block of energy usage. The effect of this energy block design, combined with the Company's proposed increase in customer charge, is substantially above average increases for lower usage customers. See, Data Filing Requirements, Part IV, Attachment IV-D-1, p.4. Under the ALJ's customer charge proposal, energy block design proposal, and proposed increase, the OCA submits that lower usage customers will still see a disproportionately large increase, just as they did under the Company's proposal.

The only reason provided by the Company for its proposal is that it wishes to recover additional customer costs in the initial blocks. The OCA submits that this proposal is, in essence, nearly the same as recovering all identified costs in the customer charge. But as OCA witness Johnson's analysis in this proceeding demonstrated, the Company's determination of

²⁴ The ALJ also noted that his proposed increase in the customer charge was "something like the rate of inflation over the last ten years." The OCA submits that this is insufficient justification for increasing the residential customer charges by 35% or more when these changes are not justified on a cost basis.

customer costs is overstated. OCA St. 3 at 25-26. In addition, as Dr. Johnson points out, the Company's proposed customer charge, combined with the higher level of recovery in the initial blocks, produces even greater revenue than what the Company claimed was customer related. The Company had calculated a customer related monthly cost of \$17.51, while the Company's proposal produces a monthly revenue of \$20.40--greater than the Company's overstated customer cost. OCA St. 3 at 26.

The OCA submits that the Company has not provided adequate justification for introducing yet another declining block in the residential rate. For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 309-310, and Reply Brief at 130-131, the ALJ's recommendation to accept the Company's proposal to introduce a third energy block should be rejected.²⁵

EXCEPTION 20: Rate Schedule ISA (R.D. 254 to 255)

At pages 254 to 255, the ALJ recommends that the Company's proposal to provide virtually no increase (0.15%) to the ISA class be accepted. PP&L had exempted the ISA class from an increase, even though the class had a rate of return at present rates of 0.79% under the Company's study, as compared to the Pa. jurisdictional return of 7.31%. The Company's proposal is based on a contract that it entered into with Bethlehem Steel Corporation, the only

²⁵ In its Main Brief, PP&L also argued that if its proposal to increase the customer charge is rejected, then any costs not recovered in the customer charge should be shifted to the first billing block based on 200 kwh usage. PP&L M.B. at 251-252. The OCA submits that as noted above, the Company's current customer charge is sufficient to recover all costs so there would be no costs unrecovered to shift to this first billing block. To the extent the Company seeks to recover its own calculation of customer charges in the first billing block, the OCA submits that this, in effect, is the same as granting the Company an increased customer charge based on its flawed analysis. This proposal should be rejected.

ISA customer, in 1988. The ALJ recommended that this contract rate be retained based on PP&L's theory of meeting competition and retaining load.

Initially, the OCA would note that PP&L presented no evidence in this proceeding to support the conclusion that the continuation of this steeply discounted rate is necessary at this time to meet competition or retain load. The Company's only evidence regarding this rate class was that it created the rate, in 1988, in response to the end-use environment and customer needs for lower rates. PP&L St. 8-R at 41. This evidence does not address the issue of the need for continuation of this steeply discounted rate.

As the OCA discussed in its Main Brief, it is within the Commission's discretion to set a just and reasonable rate for this customer class in this case. This discretion is not, and cannot, be divested by the contractual rate which PP&L and Beth Steel agreed to in 1988. See, e.g., Pa. P.U.C. v. Roaring Creek Water Co., 73 Pa. PUC 373, 431 (1990) and Lackawaxen Water & Sewer Co. v. Pennsylvania Public Utility Commission, 85 Pa. Commw. 377, 481 A.2d 1386 (1984).

The OCA submits that the evidence of record in this case, particularly the cost-of-service studies presented in this proceeding, provide ample justification for the Commission to assign a larger percentage increase to the ISA class. For example, as noted above, under the Company's cost-of-service study, the ISA class has a rate of return of 0.79% compared to the system average rate of return of 7.31%. Under the OCA's cost-of-service study, the ISA class has a rate of return that is negative, -1.69% as compared to the system average of 7.31%. Even under PP&L's 1 CP cost of service study, the methodology preferred by Beth Steel's witness Brubaker, the ISA class' rate of return is only about 40% of the system average return.

PPLICA St. 7 at 22. The OCA submits that these cost of service study results provide ample evidence of the reasonableness of increasing the ISA class by more than 0.15% when the system average increase is 11.7%. The OCA submits that the evidence of record fully supports the justness and reasonableness of increasing the revenue allocation to the ISA class to better reflect these cost of service study results.

For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 293-294, and its Reply Brief at 126-127, an increase greater than the 0.15% proposed by PP&L, at its full revenue request level, is warranted for the ISA class and should be approved by the Commission in this proceeding.

EXCEPTION 21: EDI/IDI Credits (R.D. 255 to 261)

The OCA, under the heading of Revenues, had recommended an adjustment to the Company's revenues to reflect a sharing between ratepayers and shareholders, of the revenue shortfalls resulting from the provision of discounted rates to industrial customers under PP&L's EDI/IDI programs. The Company has been providing these discounts to its industrial customers since 1987. In this case, the Company seeks to recover from ratepayers \$23,705,606 in EDI costs and \$1,625,464 in IDI costs. OCA St. 5 at 15. The OCA proposed a 50/50 sharing of these costs, which increases the Company's pro forma revenues by \$12,665,535. The ALJ rejected the OCA's proposal, largely because he found the programs to be cost-justified. R.D. at 260. The ALJ recognized the burden this places on "so-called captive customers" but accepted that burden for the purposes of this case. R.D. at 260.

The OCA submits that its proposal in this case represents an appropriate sharing of the costs of this program which provides shareholder, as well as ratepayer, benefits. Indeed, as

OCA witness Johnson testified, it is possible that PP&L's shareholders benefitted from the sales that PP&L asserts were retained by these programs since 1987, while some of that benefit has come at a cost to PP&L's other ratepayers during that period. Notably, the additional sales imposed fuel costs on the PP&L system that were equal to the marginal cost of fuel on the PP&L system, thus raising the average cost of fuel that is passed through the ECR to other ratepayers. OCA St. 5 at 17. Moreover, PP&L's shareholders will continue to benefit from the increased sales made under these programs after this rate case until the Company's next rate case.

In addition, as the OCA set forth fully in its Main Brief, the Company's evidence setting forth a cost justification, or benefit to other ratepayers, from these programs is seriously flawed. The Company's analysis merely assumes that all 300 million kwh would have been lost without the EDI/IDI program. Dr. Johnson explained the problem as follows:

This assumes that every KWH of sales for which EDI/IDI credits were provided would have been lost at the standard rate and that there were no free riders. PP&L has made no attempt to show this is the case. It simply claims that these sales would not have been made absent the EDI/IDI credit.

OCA St. 5 at 16. The OCA submits that it is improper to simply assume that all of the load would have been lost without the full rate discount.

Several states have recently adopted a sharing approach for revenue shortfalls that result from economic development rates, or load retention rates. In a 1994 case, the New York Public Service Commission found it reasonable for shareholders to absorb part of the lost margin resulting from discount rates. Re Competitive Opportunities Available to Customers of Electric and Gas Services, 154 PUR4th 19, 25 (N.Y.P.S.C. 1994). In reaching its conclusion, the New York Commission stated:

When the flexible rates induce a customer to remain on the system or acquire new load, both ratepayers and shareholders benefit, because a revenue stream covering incremental costs and contributing to common costs is maintained and the potential for stranded investment is diminished. Since both ratepayers and shareholders benefit compared to the alternative of lost load and revenue margin, it is proper for both to bear a portion of the reduced margins. This approach is a reasonable response to the significantly changing landscape of the electric industry.

Id. at 25. See also, Re Detroit Edison Co., 149 PUR4th 161 (Mich. P.S.C. 1994); Re Detroit Edison Co., 160 PUR4th 132 (1995).

An additional reason for requiring shareholders to absorb a portion of the revenue shortfall was identified by Sierra Club witness Biewald. As Mr. Biewald testified:

To the extent that utility shareholders absorb some of the revenues that are lost as a result of economic discount rates, the utility will have an incentive to minimize the amount of the discount rate, through negotiations with the customer and cost-effective DSM.

Sierra Club St. 1 at 7. Commissioner Hanger also recognized this principle when he recently stated:

Unless the shareholders of **utilities** are potentially at risk for some of the revenue that is lost as a result of the discounts **utilities** may offer pursuant to the new authority this Commission **may give**, **utilities** will not have a strong incentive to limit as much as possible the amount of lost revenues. To protect both core ratepayers and shareholders, utilities must limit as best it can the amount of revenue lost.

Pennsylvania Electric Company Supplement No. 96 to Tariff Electric-Pa. P.U.C. No. 75, Docket No. R-00943280, FEB-95-OSA-1016, Statement of Commissioner John Hanger (Revised) (emphasis in original).

Commissioner Hanger also noted in that statement that utilities should not expect to recover all of its lost revenue from ratepayers. Commissioner Hanger stated:

Permitting a utility to negotiate terms which result in lower revenue to the utility

does not mean that the shifting of **lost revenues from** such contracts to other classes of customers without any shareholder contribution to that cost **should be approved**.

Id. (emphasis in original).

For the reasons set forth above, and for the reasons set forth in the OCA's Main Brief at 86-93, and the OCA's Reply Brief at 42-43, the OCA submits that the ALJ's recommendation should be rejected, and the OCA's revenue adjustment of \$12,665,535, which reflects a 50/50 sharing of the revenue shortfalls from the provision of discounted rates under the EDI/IDI program, should be adopted.

EXCEPTION 22: ECR Proposal (R.D. 266 to 275)

At pages 266-275, the ALJ discussed several ECR issues including the Company's proposal to recover the capacity costs associated with expiring off-system sales, such as the sale of 945 MW of capacity to JCP&L, through its ECR. The ALJ properly rejected the Company's proposal. The ALJ, however, adopted the Company's alternative proposal. Under the alternative proposal, the Company recommended that if ECR recovery of the capacity related costs was denied, then all revenues from off-system capacity-related sales should also be excluded from the ECR and treated as an element of base rates in this case. In addition, PP&L asked that it be granted authority, in this case, to retain the energy savings related to this returning capacity, if its proposal is denied.

The OCA does not object to the ALJ's approval of PP&L's proposal to exclude off-system sales from the ECR and treat them as an element of base rates. However, the ALJ did not reflect the approximately \$20.8 million of revenues from these sales in base rates in determining the Company's pro forma revenues. Consistent with the ALJ's recommendation,

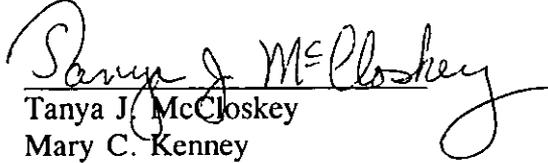
the approximately \$20.8 million of off-system sales reflected in the Company's filing as a credit in the ECR must now be reflected as an adjustment to increase pro forma revenues. The OCA would except to the failure to recognize this adjustment to revenues in the event that the ALJ's recommendation is accepted by the Commission.

The OCA also excepts to the ALJ's approval, in this proceeding, of the Company's proposal to retain the energy savings associated with this capacity in any future ECR cases. The OCA is not arguing at this time that the Company be prohibited from retaining these energy savings. Rather, the OCA's position is that it is premature to rule on this request at this time when the full circumstances surrounding the appropriateness of such request cannot be known. The OCA submits that the Company should appropriately request this relief in an ECR proceeding at the time it is required where the proposal can be evaluated based on the circumstances at that time. A blanket advanced approval of this proposal would mean that PP&L can selectively determine which ratemaking treatment is most profitable. OCA St. 2A at 35. The OCA submits that the Company should retain the right to file for such relief in an individual ECR case, but should not be given a blanket approval to utilize this treatment indefinitely without regard to the relevant facts at the time.

III. CONCLUSION

WHEREFORE, OCA respectfully submits that the ALJ erred in his recommendations with respect to the above issues and his decision on those issues should be rejected in favor of the positions advocated by the OCA in this proceeding and discussed above.

Respectfully submitted,



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CERTIFICATE OF SERVICE

Re: Pennsylvania Public Utility Commission
v.
Pennsylvania Power and Light Company
Docket No. R-00943271

I hereby certify that I have this day served a true copy of the foregoing document, Office of Consumer Advocate's Exceptions, 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 August, 1995.

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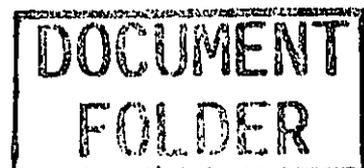
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VIA HAND DELIVERY

In re: **Pennsylvania Public Utility Commission, et al., v. Pennsylvania Power & Light Company; Docket No. R-0943271**

Dear Secretary Alford:

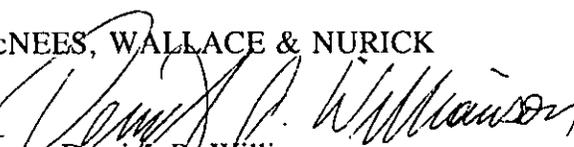
Enclosed please find the original and nine (9) copies of the Exceptions of the PP&L Industrial Customer Alliance. All parties of record have been duly served as evidenced by the attached Certificate of Service.

Please date stamp the enclosed copy of this transmittal letter and kindly return for our filing purposes.

Very truly yours,

McNEES, WALLACE & NURICK

By


Derrick R. Williamson

DPW/mts
Enclosures

cc: Certificate of Service

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BEFORE THE
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COMMISSION, ET AL.,

v.

PENNSYLVANIA POWER & LIGHT
COMPANY

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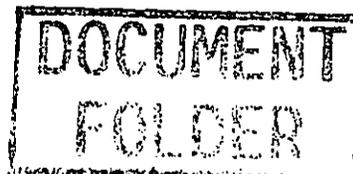
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DOCKETED

AUG 14 1995

Counsel for PP&L Industrial
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Dated: August 14, 1995



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I. INTRODUCTION

Administrative Law Judge ("ALJ") Robert A. Christianson issued a Recommended Decision ("R.D.") in this proceeding on July 31, 1995. The PP&L Industrial Customer Alliance ("PPLICA"), an active participant during the evidentiary phase of the proceeding before ALJ Christianson, respectfully excepts to certain portions of the ALJ's Recommended Decision pursuant to 52 Pa. Code § 5.533.

Specifically, PPLICA excepts to the following recommendations of the ALJ:

- (1) That Pennsylvania Power & Light's ("PP&L" or "Company") proposed rate design for large interruptible customers be approved without adjustment (beyond cost of service and allocation adjustments) (R.D., p. 251);
- (2) That PP&L's "valuation" of interruptible load for cost of service study purposes is proper (R.D., p. 206);
- (3) That the approved base rate increase equates to approximately \$61 million, rather than \$40 million pursuant to a PPLICA adjustment (see R.D., pp. 273-75).
- (4) That PPLICA's proposal to utilize a historic test year for capital structure purposes be rejected (R.D., pp. 143, 158-59);
- (5) That PP&L's proposal to levelize the modified sinking fund depreciation for its Susquehanna Units be approved (R.D., pp. 114-15);
- (6) That PP&L's request to increase its allowed annual nuclear decommissioning accrual be approved (R.D., p. 99);
- (7) That PPLICA's adjustments to PP&L's recovery of the cost of its Voluntary Early Retirement Program be denied (R.D., pp. 44-45); and,
- (8) That PP&L's proposal to recover costs related to Statement of Financial Accounting Standards No. 106 be approved (R.D. p. 50).

PPLICA excepts to the ALJ's Recommended Decision with respect to the conclusions set forth above, and in support of those exceptions, PPLICA incorporates by reference applicable portions of its Main Brief and Reply Brief, and provides additional reasons as per 52 Pa. Code § 5.533.

II. EXCEPTIONS

1. **The ALJ Erred In Approving A Rate Design For Interruptible Customers Which Will Impose An Increase, On Average, of 22% to 28% To Those Customers.**

a. **Introduction.**

The Company proposed two separate industrial rate classes, LP-5 and LP-6, containing four different rate schedules, LP-5 firm, LP-5 interruptible, LP-6 firm, and LP-6 interruptible. The Company's proposal for interruptible rates under LP-5 and LP-6 is essentially the application of a flat \$/kW "interruptible credit" which is applied to the LP-5 and LP-6 firm rates. That interruptible rate, or credit, is calculated utilizing a "resource value approach" which assumes that interruptible load is a substitute for peaking capacity; the Company based its interruptible credit on the cost of a new combustion turbine peaking unit and proposed an interruptible credit of \$6.00/kW per month and \$8.00/ kW per month, depending upon notice requirements. By proposing a flat \$/kW interruptible credit, PP&L dramatically modified its historic interruptible rate design by removing the currently applicable demand/energy block interruptible rates. See PPLICA Main Brief, pp. 74-75.

PPLICA adamantly opposed PP&L's proposed rate design changes for the interruptible class. PPLICA Main Brief, pp. 74-80. Toward that end, PPLICA recommended a rate design recognizing three separate and distinct rate schedules: LP-5 firm, LP-6 firm and LP-5/6 interruptible. The LP-5/LP-6 interruptible schedule would retain PP&L's existing LP-5 interruptible rate structure; i.e., PP&L's proposal to provide an

interruptible credit based upon a "resource value approach" is not applied, and the existing demand/energy blocked rates for LP-5 interruptible customers would be maintained.

Consequently, PPLICA's recommended revenue allocation (based on the goal of achieving a 50% reduction in existing subsidies for each rate class and moving all rates toward the system average rate of return) provided that no rate schedule, including the interruptible rate schedule (pursuant to PPLICA's design), would receive an increase in excess of 1.5 times the authorized system average increase, consistent with the principle of gradualism in ratemaking. *Id.* at 61-64.

The ALJ adopted PP&L's rate design proposal for the LP-5 firm, LP-5 interruptible, LP-6 firm, and LP-6 interruptible rate schedules, and rejected the PPLICA proposal. R.D., pp. 250-51. The ALJ specifically concluded that, for ratemaking purposes, PP&L's value of service approach (utilizing a combustion turbine as a measure of costs saved) was the appropriate approach for determining the value of the interruptible load credit. *Id.* at 206. The ALJ also generally adopted the PP&L revenue distribution proposal. *Id.* at 226.

The ultimate impact of the ALJ's recommendation is that, based upon PP&L's assessment that interruptible customers were to receive a 22% rate increase (under PP&L's rate design) even if PP&L were afforded no base rate relief (PPLICA Statement No. 1, Exh. PFC-1; tr. at 2202-03) and at least a 28% increase if PP&L were given full rate relief (tr. at 774), current LP-5 interruptible customers will receive an increase somewhere between 22% and 28%, despite the fact that the ALJ's recommendation results in a system average

increase of only 2.7%. PPLICA takes vociferous exception to the ALJ's recommendation which has the effect of singling out interruptible customers for rate increases which will be nearly **TEN TIMES** the system average rate increase of 2.7%!

b. The ALJ erred in approving a rate design which results in rate increases violative of the principle of gradualism.

As aforementioned, the ALJ approved PP&L's rate design for the industrial classes which identifies four separate rate classes (LP-5 firm, LP-6 firm, LP-5 interruptible, and LP-6 interruptible) but then combines them into only two rate schedules (LP-5 Firm/Interruptible, LP-6 Firm/Interruptible) for tariff application purposes. That design replaces the traditional optional interruptible power provision of the tariff with an interruptible credit (that credit being based on a truncated value of service measurement as opposed to a traditional embedded cost of service measurement) which is applied to the LP-5 and LP-6 firm rates. The currently applicable, PUC approved, demand and energy blocked rates are discarded under PP&L's design, in favor of PP&L's proposed flat \$/kW rate with an adjustment for load factor. PPLICA Main Brief, p. 74; tr. at 2215. This change in design leads to the substantial rate increase for customers receiving service under the interruptible rate schedule referenced above. Tr. at 804-06.

As aforementioned, according to PP&L witness Kasper, if PP&L were to be granted no increase, but its rate design for LP-5 interruptible customers were approved, those customers would still receive an overall increase of over 22%! PPLICA Statement No.1,

Exhibit PFC-1. Similarly, if PP&L were granted full relief, LP-5 interruptible customers would receive a 28% rate increase under the Company's rate design. As such, the effect of the ALJ's approval of the PP&L rate design and a recommended increase of approximately \$61 million is a rate increase to interruptible customers of between 22% and 28% (in accord with PP&L witness Kasper's analysis contained in Exhibit PFC-1 of PPLICA Statement No. 1). Given that the system average increase under the ALJ's recommendation is approximately 2.7%, the effective rate increase to the interruptible class will be **ten times the system average increase**. Imposing an increase of that magnitude on any class or group of ratepayers is flatly unreasonable. Moreover, PPLICA excepts to the ALJ's recommendation to approve the PP&L rate design, as that design leads to rate increases violative of the gradualism principle to which this Commission adheres.

As PPLICA established in its Main Brief, the Commission has routinely recognized that in order to avoid rate shock, rate increases must be effected in a gradual manner. PPLICA Main Brief, p. 67; See Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 74 PaPUC 1, 211-12 (1990). The Commission has specifically stated: "[i]t is well established in utility ratemaking that class cost of service studies serve as a guide . . . in the formulation of rate structure. Other factors such as gradualism and competitiveness must be considered as well." Pennsylvania Public Utility Commission v. National Fuel Gas Distribution Corporation, 73 PaPUC 552, 621 (1990) (emphasis added). Indeed, the Commission has specifically recognized the principle of gradualism in identifying

and adopting proper rate structure proposals. See Pennsylvania Public Utility Commission v. Western Pennsylvania Water Company, 95 PUR4th 470, 515-16 (1988); Pennsylvania Public Utility Commission v. Pennsylvania-American Water Company, 97 PUR4th 469, 507-08 (1988).

PP&L has itself recognized and alleged that it supports gradualism in ratemaking. PP&L Statement No. 8, p.5; PP&L Statement No. 1, p.3. Toward that end, PP&L's own proposal attempted to "cap" rate class increases at 1.5 times the system average increase, and PP&L acknowledged that a 20% increase to any one class would violate the principle of gradualism (though PP&L refused to acknowledge that interruptible customers were a separate class to be protected by this cap). PPLICA C.E. Exhibit No. 6; Tr. at 775. Even the ALJ recognized the importance of gradualism in ratemaking. R.D., p. 210.

Despite this, the ALJ has approved a rate design which will result in a substantial increase to the interruptible class. That increase, between 22% and 28% (and 10 times the system average increase under the ALJ's recommendation), clearly violates the principle of gradualism in ratemaking. Recall, even PP&L acknowledged that a 20% increase would violate the gradualism principle. Tr. at 775.

The only justification provided by PP&L and the ALJ for this disparate treatment is the assertion that interruptible customers are not a separate class.¹ Indeed, the ALJ states:

¹ PPLICA proposed a rate design which would treat the LP-5 and LP-6 interruptible customers as a separate class (PPLICA Statement No. 7, pp. 59-64; PPLICA Main Brief, pp. 74-77); the ALJ expressly rejected the proposal (R.D., p. 209).

I view the interruptible customers as simply customers within the general class and not as a separate class. They take service like other industrial customers and, to some degree, allow interruption. [Though] interruption might often be more a theoretical possibility than a real problem.

R.D., p. 251 (emphasis added).

The ALJ's conclusion is incorrect. PP&L's interruptible customers should constitute a separate class (consistent with the PPLICA rate design proposal) as they receive a service that is decidedly inferior in quality as a result of the prospect of interruptibility. Toward that end, contrary to the assertion of the ALJ, interruption is a reality, not just a theoretical possibility; shortly after the ALJ issued his decision, various large industrial customers receiving interruptible service from PP&L curtailed consumption pursuant to a request from PP&L as result of record usage during the week of July 31 through August 4, 1995. "PP&L industrial customers shut down to save juice," The Tribune, Scranton, PA (August 4, 1995); "Businesses come through in the heat," Reading Times, p. B1 (August 7, 1995). This underscores the clear, practical difference between industrials receiving firm service (service without risk of interruption) and industrials receiving cheaper, yet much less reliable, interruptible service.

Moreover, under PP&L's existing Optional Interruptible Power provision of LP-5, customers selecting interruptible service are imposed explicit demand/energy charges which differ from the LP-5 firm demand and energy charge. PP&L's existing rate design recognizes that interruptible customers are essentially a separate class.

Consequently, there should be a separate rate category for PP&L's industrial interruptible customers, consistent with the PPLICA proposal in this proceeding. PPLICA Statement No. 7, p. 60; PPLICA Main Brief, pp. 76-77. As such, there is absolutely no justification for foisting a 22%-28% rate increase upon interruptible customers in violation of the principle of gradualism.

Even if interruptible customers are not deemed a separate class, this Commission cannot allow PP&L to subject these customers to the type of increase and manipulation that PP&L has attempted to implement (and the ALJ has implicitly recommended). Even the ALJ recognized that the keeping of interruptible customers within their fundamental classes can give rise to manipulation (R.D., p. 209), though, unfortunately, he approved the PP&L rate design in any event. The gradualism principle applies to all utility customers, not just classes of customers. No customers should be subjected to rate increases that are ten times the system average increase. The ALJ erred in recommending a rate design which manipulates interruptible rates to the tune of a 28% increase in violation of the gradualism principle.

- c. **The ALJ erred in approving an interruptible rate design which fails to acknowledge and address prevailing competitive exigencies.**

PPLICA argued in its briefs that PP&L's rate design proposal was in diametric opposition to prevailing competitive trends insofar as the PP&L proposals were intent upon foisting a massive rate increase onto the industrial interruptible class, despite the competitive

pressures facing large industrial customers and despite increasing competition in the electric industry itself. PPLICA Main Brief, pp. 64-70; PPLICA Reply Brief, pp. 3-7, 10-15. Despite PPLICA's argument, as aforementioned, the ALJ approved the PP&L rate design and the concomitant 22%-28% rate increase (based on PP&L witness Kasper's previous analysis) for large interruptible customers. PPLICA excepts to the ALJ's recommendation on the basis of the ALJ's failure to fully recognize the detrimental competitive impact of the interruptible rate increases to the industrial class.

As PPLICA established in its Main Brief, electric utilities and public utility commissions on a national scale are making efforts to address competition in the electricity industry and the competitive alternatives that are available to large industrial customers. Initiatives in California, Michigan, Massachusetts, Louisiana, and at the Federal Energy regulatory Commission, are but a few examples of this national trend. See PPLICA Main Brief, pp. 65-66. The Pennsylvania Commission has also recognized the competitive trend in the utility industry, having very recently issued an initial report on electric competition. Investigation Into Electric Power Competition, I-940032.

The PUC has also recognized the need to address both competition as it affects the utility industry and competition as it affects utility customers. Indeed, as Chairman Quain stated in dissent to the PUC's approval of PP&L's closure of its interruptible service offering earlier this year: "Interruptible service offerings within this Commonwealth have been an excellent tool to encourage economic development, as well as the retention of current load. *

* * We must remain cognizant of the increasing pressures which face business customers of PP&L, as well as the utility itself." Pa.P.U.C, et al., v. Pennsylvania Power & Light Co., Docket No. R-00943081, Opinion and Order entered February 9, 1995.

Toward that end, the Commission has recognized the propriety of allowing utilities to offer, modify and/or classify services for the benefit of generic and individual customer economic development and business needs. See, e.g., Pa. P.U.C. v. Peoples Natural Gas Co., 57 Pa PUC 555 (1983) (approving experimental competitive energy rate designed to retain and regain industrial sales); Re West Penn Power Co., 63 Pa PUC 557 (1987) (approving waiver of demand ratchet clause where industrial customer needed to meet temporary increase in the market demand for its product).

More specifically, the Commission has expressly recognized the need to consider the protection of the economic interests and competitive positions of utility customers for the benefit of the public interest. In Re: Lukens Steel Company, 58 Pa PUC 256 (1984), affirmed, Lukens Steel Company v. Pennsylvania Public Utility Commission, 92 Pa. Cmwlth 530, 499 A.2d 1134 (1985), Lukens Steel Company sought a declaratory order from the Commission approving its purchase of PP&L delivery facilities for the purpose of receiving electric supply service from PP&L, as opposed to PECO, in order to reduce energy related production costs and thereby increase its own competitiveness. In assessing whether Lukens' proposed purchase was in the public interest, the Commission stated:

Lukens has . . . presented evidence in support of its contention that its proposal is in the public interest. This evidence consists of the employment impact which allegedly would result from a denial of its petition. **The matter of the economic impact of a denial of Lukens' request is certainly germane to the public interest issue, and this Commission is greatly concerned with any issue which has economic and employment consequences.**

58 Pa PUC at 264 (emphasis added). Although the Commission ultimately denied Lukens' proposal, it clearly gave full consideration, pursuant to its duty to protect the public interest, to Lukens' economic interest and competitive position. Similarly, the Commission in Lewistown Specialty Yarns, Inc., v. Pennsylvania Electric Co., Docket No. C-00924069, Opinion and Order entered May 24, 1994, specifically addressed the competitive concerns of the complainant, a utility customer.

The Commission has recently reaffirmed that the Public Utility Code requires that the Commission, in carrying out its charge to protect the public interest, must recognize that the impacts of rates on utility customers who operate in competitive markets is a relevant issue that must be considered and addressed. Specifically, the Commission noted in Pennsylvania Public Utility Commission, et al. v. UGI Utilities, Inc. -- Gas Division, Docket No. R-00943064, Opinion and Order entered November 30, 1994, that it has often acknowledged the adverse consequences to all ratepayers brought about by the loss of large industrial customers, and the Commission specifically stated in evaluating the impact of proposed rates on large industrial customers that "[t]he effect that the rates established in this proceeding

will have on each of these Companies in its competitive market is relevant to this proceeding."

Finally, in addition to Commission precedent which clearly recognizes that the competitive concerns of utility customers are relevant in proceedings before the Commission, Chairman Quain of the Commission very recently outlined at Public Meeting that such considerations are part of a broader Commission policy. Specifically, he stated, in keeping with Governor Ridge's pledge to make Pennsylvania a better place for business: "We seek to work together to pursue economic development initiatives where appropriate to maintain and attract jobs to Pennsylvania, to make sure that we work for the benefit of all of our citizens and our businesses within this Commonwealth." See p. 11, Transcript of the Public Meeting held March 16, 1995.

In short, the Commission has unequivocally recognized, as a matter of both policy and precedent, that the economic interests and competitive positions of utility customers are relevant to Commission deliberations regarding the effects of utility rates and services.

With that in mind, the rate design proposal approved by the ALJ constitutes a giant step backward for this Commonwealth's economic development and retention programs by unnecessarily imposing a significant, adverse rate increase upon industrial users of PP&L's interruptible service. This is especially alarming given that no less than six industrial companies provided impact testimony in this proceeding detailing the importance of low electric rates. See PPLICA Statements Nos. 1-6. Apparently, the ALJ ignored that testimony

despite several explicit references in PPLICA's Main Brief. The following passage from

PPLICA's Main Brief is dispositive of the competitive concerns of large industrial customers:

For many of these companies, electricity costs represent upwards of 70% of total production costs. See PPLICA Statement No. 1, p. 3 (BOC Gases); PPLICA Statement No. 2, p. 4 (Air Products). Obviously, an increase of the magnitude proposed by PP&L will seriously impinge upon these companies' respective costs of production and may ultimately hasten their departure from the PP&L service territory and concomitant losses to the local and state economies.

Similarly, many of these companies served by PP&L have plants in other states which are essentially in competition with the plants here. See PPLICA Statement No. 3, pp. 5-6 (Donnelley); PPLICA Statement No. 4, pp. 4-5 (Hershey). Many of these companies must remain globally competitive as well. See, e.g., PPLICA Statement No. 5, p. 4 (Thomson). To the extent that PP&L significantly raises interruptible rates under which these companies receive electricity, their ability to make their Pennsylvania investments profitable enough to outpace sister plants and competitors will be seriously impaired. Again, the risk of loss to the economy of the Commonwealth and the risk of loss for the PP&L system is enhanced.

Finally, to the extent that PP&L pursues its campaign to hike interruptible industrial rates, individual PPLICA members can only be left to assume that the metaphorical welcome mat has been pulled out from under them. This is alarming not only because it indicates a total reversal of PP&L's position from 1992 when it first proposed its Optional Interruptible Power service, but because these companies may be left no recourse but to pursue any and all competitive alternatives. See PPLICA Statement No. 6, pp. 7-9 (Armstrong).

PPLICA Main Brief, pp. 68-69.

PPLICA members consume in excess of 2.4 billion kWh of electricity on the PP&L system at a cost over \$105 million. PPLICA members employ over 26,000 people in PP&L's service territory, purchase over \$230 million in goods and services from the local

economy, and pay nearly \$64 million in state and local taxes. PPLICA Main Brief, pp. 1-2. To the extent that the ALJ's decision unfairly foists a 22%-28% increase upon industrial customers, the contributions that PPLICA members make to this state's economy are placed at risk. The Commission simply cannot afford to ignore PPLICA's testimony when determining the appropriate increase to PP&L's interruptible customers.

The ALJ's recommendation is particularly offensive to PPLICA given that the ALJ accepted PP&L's "theory of meeting competition and retaining load" in approving PP&L's special contract with Bethlehem Steel (that contract assuring that Bethlehem Steel receives essentially no rate increase in this proceeding) (R.D., p. 255), while implicitly rejecting PPLICA's claims, as advanced through the impact testimony of six witnesses, that the massive interruptible rate increase proposed by PPLICA was extremely detrimental to the competitive business interests of both PPLICA members and the Commonwealth as a whole. It is wholly inconsistent for the ALJ to ratify a special contract with a single large customer on the basis of a "theory of competition," while effectively ignoring that same theory of competition in approving an interruptible rate design for numerous industrial customers (whose contributions to the local and state economy and tax base are significant) that will lead to rate increases to these customers approaching ten times the system average increase.

Given the competitive exigencies faced by individual PPLICA members, and prevailing competitive trends throughout the utility industry, the ALJ's approval of a rate design which will result in increases to industrial customers of 22%-28% (or ten times the

system average increase) is clearly erroneous. The Commission must recognize that the reasonable protection of the competitive business interests of this Commonwealth serves the public interest. The PUC should limit any rate increase for the interruptible class to 1.5 times the system average increase as per the PPLICA rate design and revenue distribution proposal. See PPLICA Main Brief, pp. 61-64, 74-77.

d. The ALJ erred in approving a rate design based upon a flawed "resource value approach."

As aforementioned, PP&L proposed a rate design which eliminates a separate interruptible tariff and replaces it with an "interruptible credit" which is applied to firm rates (on both LP-5 and LP-6, as proposed by PP&L). That credit is determined utilizing the "resource value" or "value of service" approach, and PP&L proposed basing the credit on the cost of a new combustion turbine peaking unit. See PPLICA Main Brief, p. 74. PP&L identified interruptible credits of \$6.00/kW and \$8.00/kW (depending upon notice requirements) based on its proposal.

Despite PPLICA's opposition, the ALJ approved PP&L's rate design proposal, and the ALJ specifically approved the implementation of the "value of service" (also referred to as the "resource value") approach to ratemaking for interruptible service based upon a peaking capacity proxy. R.D., pp. 206, 250. PPLICA adamantly opposed PP&L's rate design proposal in general, and specifically opposed PP&L's use of a "resource value approach" to identifying an interruptible credit (PPLICA Main Brief, pp. 78-80); PPLICA

therefore excepts to the ALJ's approval of PP&L's "value" approach for rate design purposes.

As PPLICA argued in its Main Brief (pp. 78-80), under PP&L's rate design, interruptible customers who desire to purchase lower quality power are being told that they are, in effect, buying firm power and selling back peaking capacity to PP&L. However, these interruptible customers have no true market for the sale of their "peaking capacity"; i.e., interruptible customers must sell their capacity to PP&L, thus PP&L is a monopsonist (a single buyer of a product marketed by a number of sellers) able to drive the price (or value) of peaking capacity down. PPLICA Main Brief, pp. 78-79. As the monopsonist, PP&L can undervalue the peaking capacity provided by interruptible customers. As such, the "value" approach proposed by PP&L (which assumes that interruptible service is merely a substitute for peaking capacity) is inherently flawed and should be rejected.

It is instructive to note that in approving the "value" approach to ratemaking, the ALJ stated: "Especially as a utility enters the competitive arena, value of service (what the market will bear) must become relatively more important, in comparison to cost of service analysis." R.D., p. 250. Despite this analysis, the ALJ failed to insure that the approach used to value the service at issue was truly indicative of "what the market will bear": A market ruled by a monopsonist should not be the type of market used to value service.

PP&L's value approach is not only flawed because it is based upon a monopsonist-controlled measure, but also because that valuation fails to include an adjustment for active

load management which would raise the value of interruptible load to reflect a reserve margin which is avoided when interruptible load is on the system. PPLICA Main Brief, p. 79; PPLICA Statement No. 7, p. 67.

Moreover, contrary to the assertions of the ALJ, the fact of interruption is real and valuable. In apparently attempting to justify approval of PP&L's faulty peaking capacity/value of service approach, the ALJ stated as follows:

PP&L does not fully control interruptible customers for purposes of load reduction and these customers do enjoy rather good service, especially considering the rather adequate capacity enjoyed by PP&L currently.

* * *

. . . I also agree with PP&L about its choices for ratemaking purposes. I view the interruptible customers as members of their normal classes, members who have been, for a few years, given a particular break, based on both the theoretical interruptible considerations and the more practical considerations of meeting competition and industrial development.

R.D., p. 206 (emphasis added). As aforementioned, many of PP&L's large industrial customers recently curtailed service in response to a PP&L request. Indeed, PP&L spokesman Lawrence A. Downing specifically credited large industrial customers and the "value" of their ability to shed load. Reading Times, p. B8 (August 7, 1995). Consequently, any attempts to justify undervaluing interruptible service through the application of a monopsonist-controlled peaking capacity measure must be rejected.

Finally, PP&L's value approach should also be rejected because it is wholly unfair for PP&L to require interruptible customers to pay rates based upon some subjective "value,"

while all other customers pay rates based upon embedded cost of service. PPLICA Main Brief, p. 78. PP&L and the ALJ have provided no reasonable justification for the differentiation, and given the flaws inherent in the PP&L proposal (the peaking capacity proxy), PP&L's proposed value of service rate design should be rejected. Whether the PUC employs value of service ratemaking in the natural gas industry is irrelevant to the electric industry because natural gas customers have proven, competitive alternatives (e.g., oil, coal, propane). *Electric utility customers have no comparable alternatives, and a value of service pricing philosophy will force those customers to pursue less direct alternatives, like municipalization and retail wheeling.*

e. The ALJ erred in rejecting PPLICA's proposed rate design proposal.

In adopting PP&L's rate design (for LP-5 and LP-6) proposal, the ALJ implicitly rejected PPLICA's rate design proposal, and specifically rejected PPLICA's proposal for an LP-5/LP-6 interruptible rate class. R.D., p. 209. PPLICA excepts to these recommendations.

PPLICA proposed that the current LP-5 revenue class be divided into three separate classes: LP-5 firm (consistent with the PP&L proposal), LP-6 firm (consistent with the PP&L proposal), and a single interruptible class falling under an LP-5/LP-6 Interruptible rate schedule. PPLICA Main Brief, 74-77, App. E; PPLICA Statement No. 7, pp. 59-64.

Given the flaws inherent in the Company's interruptible rate design (i.e., the design leads to unreasonably high increases in interruptible rates in violation of the gradualism principle and recognized competitive/public interest exigencies, and it is based on a flawed value of service approach), PPLICA merely proposed that PP&L's current interruptible rate design be continued. That design would continue to incorporate a demand charge applicable to billing kW, with two energy blocks also applying. PPLICA Statement No. 7, p. 62. In addition, PPLICA's proposal requested the express recognition of interruptible customers as a separate class. As aforementioned, there is no doubt that interruptible customers do constitute a separate class given the decided differences in reliability between firm and interruptible service, and the reality of interruption. PP&L's differing rate treatment of firm and interruptible customers under its current LP-5 firm and optional interruptible service provision bear this out. See pp. 8-9, supra.

Having identified the various flaws inherent in the PP&L proposal, the Commission must opt to approve the PPLICA rate design proposal as it is the only reasonable interruptible rate design proposal offered in this proceeding, PP&L having failed to provide a reasonable alternative.

Critical to the PPLICA proposal is, of course, the recognition that the LP-5/LP-6 Interruptible class is a separate class to be protected by the 1.5 times system average increase cap (advocated by PP&L, PPLICA and various other parties). PPLICA Main Brief, p. 63. Consequently, in addition to Commission approval of PPLICA's interruptible rate design, the

Commission should approve the PPLICA recommended revenue distribution proposal (or some derivation thereof) attached as Appendix D to the PPLICA Main Brief. This allocation proposal seeks to achieve a 50% decrease in interclass subsidies and recognizes the 1.5 times system average cap for rate class increases, the interruptible class being a separate class protected by the 1.5 times cap. It bears noting that PPLICA does not seek to excuse the interruptible class from any rate increase. As per PPLICA's rate design and revenue allocation proposal, interruptible customers would receive an increase that is greater than the system average increase (though no more than 1.5 times the system average increase). See PPLICA Main Brief, pp. 61-64, Appendix B. PPLICA steadfastly maintains that this treatment is reasonable, in compliance with the gradualism principle, sensitive to competitive exigencies, and otherwise in the public interest.

2. The ALJ Erred in Approving PP&L's "Resource Value" Credit for Interruptible Load for Cost of Service Study Purposes.

PP&L's cost of service study accounted for interruptible load by allocating the cost of the service to the classes having the interruptible service option under the current tariff (ISA, LP-4, LP-5), and then crediting to the respective classes the "value" of that interruptible load, such value being based upon the cost of combustion turbine peaking capacity. PP&L ascribed a "value" for interruptible load equivalent to \$3.00/kW per month. PP&L Main Brief, p. 238.

PPLICA opposed the "resource value approach" for rate design purposes (PPLICA Main Brief, pp. 74-80), but PPLICA also argued that if the resource value/credit approach is appropriate for cost of service study purposes, the \$3.00/kW per month credit utilized by PP&L in its cost of service study was understated and should have at least reflected the \$6.00 and \$8.00/kW credits proposed by PP&L in its rate design for interruptible customers. Id. at 48-50; PPLICA Reply Brief, pp. 6-7. In short, PPLICA proposed that the Company's cost of service study must be adjusted to reflect the "true" value of interruptible load; i.e., the \$6.00 and \$8.00/kW credits proposed by the Company in its rate design. PPLICA then proposed that the cost of paying these credits should be allocated to all customer classes on the basis of the 12 CP production demand allocation. PPLICA Main Brief, pp. 49-50; PPLICA Statement No. 7, p. 27.

The ALJ approved PP&L's cost of service study analysis with some modifications proposed by PPLICA. See R.D., pp. 204-10. The ALJ agreed specifically with PPLICA that the cost of the revenue credits associated with interruptible service be allocated to all classes. Id. at 207. However, the ALJ apparently accepted PP&L's \$3.00/kW per month "value" for interruptible load for cost of service study purposes. See id. at 206. PPLICA excepts to this determination.

As PPLICA explained in its Main Brief, by valuing interruptible load at only \$3.00/kW for cost of service study purposes, while proposing an actual interruptible credit (for rate design purposes) of either \$6.00 or \$8.00/kW, the Company has created a mismatch whereby customers are required to pay the difference between the \$3.00 the Company assumes for its cost of service study and the actual credits being proposed by the Company (\$6.00/\$8.00). PPLICA Main Brief, p. 49; PPLICA Reply Brief, p. 7. Neither PP&L nor the ALJ have provided any reasonable explanation for utilizing an interruptible load "value" credit of \$3.00/kW for cost of service study purposes, when PP&L has, through its rate design proposal, recognized a value for interruptible load of \$6.00/kW (two hour notice interruption) and \$8.00/kW (30 minute notice interruption). The Company's cost of service study, as approved by the ALJ, must be further adjusted to reflect an interruptible credit (or value) of \$6.00/kW (two hour notice interruptible load) and \$8.00/kW (30 minute notice interruptible load). PPLICA Main Brief, p. 49.

3. The ALJ Erred in Failing to Adjust His Recommended Increase In Operating Revenues to Reflect the Actual Increase in Annual Operating Revenues Requested by PP&L.

PPLICA argued in its briefs that PP&L's request for an increase in total annual base rate operating revenues of \$261 million was actually a request for an increase in annual operating revenues of only \$240 million. See PPLICA Main Brief, pp. 1 (n.1), 31-34; PPLICA Reply Brief, p. 30. Specifically, PPLICA argued that if PP&L's proposal to recover costs (in its Energy Cost Rate or "ECR") related to the loss of off-system sales to Jersey Central Power & Light Company ("JCP&L") was rejected, then the net base rate operating revenue increase sought by PP&L would be \$240 million, not \$261 million, because PP&L agreed that it would credit base rates with revenues associated with off-system capacity sales (credits of approximately \$21 million, PPLICA Statement No. 7, pp. 12-13) if its JCP&L proposal was rejected by the Commission. PPLICA Main Brief, p. 33; PP&L Statement No. 7-R, p.34-35. PP&L agreed with this analysis. As stated by PP&L witness Kleha:

If all else is approved, all aspects of PP&L's proposed request for a base rate increase of \$261 million is approved, but ECR recovery of non-energy revenue requirements associated with long-term bulk power sales is disapproved and, as a consequence, the off-system capacity related sales revenues associated with installed capacity credit agreements, output reservation contracts, and transmission entitlements are included back in the rate base calculation, then the overall net effect would be a net increase of \$240 million.

Tr. at 2147.²

Subsequently, the ALJ rejected the "primary" PP&L proposal to recover costs associated with lost JCP&L capacity sales in the ECR, but the ALJ recommended approval of PP&L's "alternative" proposal (requiring in part that revenues from off-system capacity-related sales are to be credited to base rates). R.D., pp. 274-75. In dealing with PP&L's proposal to recover the cost of its lost sales to JCP&L in the ECR, the ALJ referenced PPLICA's assertion that PP&L is actually requesting an increase in base rates of only \$240 million (R.D., p. 273); however, the ALJ apparently failed to expressly address the issue of adjusting PP&L's actual proposed increase. Given that the ALJ directed the parties to point out to the Commission (in Exceptions) any significant issues which he may have missed (R.D., p. 189), PPLICA must except to the ALJ's decision insofar as it fails to identify the proper increase in revenues requested by PP&L.

The ALJ has recommended rejection of PP&L's JCP&L ECR proposal and approval of the treatment of off-system sales revenues in base rates. As such, PP&L's requested annual operating revenue increase is \$240 million (resulting from the credit to current rates of approximately \$22 million for off-system sales). PPLICA Statement No. 7, pp. 11-12,

² As PPLICA also noted in its briefs and testimony, even if PP&L's JCP&L cost recovery proposal was accepted by the Commission, the net increase to ratepayers (if PP&L were granted its entire request) would still be \$240 million because of a \$21 million credit to the ECR. PPLICA Main Brief, pp. 32-34; PPLICA Reply Brief, p. 30; PPLICA Statement No. 7, pp. 12-13. PP&L was in agreement with this analysis as well. Tr. at 2148. Thus a \$21 million adjustment to PP&L's request is necessary in any event.

77; Tr. at 2147; PPLICA Main Brief, pp. 31-34; PPLICA Reply Brief, p. 30.

Unfortunately, the ALJ's ultimate recommendation for increases to the total annual operating revenues for PP&L failed to incorporate this correction. Table 1 of the ALJ's Recommended Decision indicates "pro forma present rates" (in thousands of dollars) of \$2,401,887.00 and total allowable operating revenues of \$2,463,631.00, resulting in an ALJ approved increase to revenues of \$61 million. However, the ALJ failed to credit pro forma present rates as per the alternative proposal he approved at R.D., p. 275 (and as per the PPLICA argument). To correct this error, the ALJ's pro forma present rates should be approximately \$2,423,000.00 (to account for the crediting to base rates of approximately \$22 million in revenues; PPLICA Statement No. 7, p. 12) which, when contrasted with total allowable revenues of \$2,463,631.00, results in an ALJ approved increase of approximately \$40 million, not \$61 million. The ALJ's Recommended Decision must be corrected consistent with this analysis.

4. The ALJ Erred in Adopting a Capital Structure Based Upon a Future Test Year.

PP&L's rate of return proposal in this proceeding was based upon a capital structure for the 1995 future test year period which incorporated the effects of a speculative equity issuance scheduled for August, 1995. Tr. at 52-53; PPLICA Main Brief, pp. 27-28.

PPLICA opposed PP&L's use of a capital structure that was based upon a speculative equity issuance and proposed a capital structure based upon the 1994 historic test year. PPLICA Main Brief, pp.27-28. The ALJ concluded that reliance upon PP&L's proposed capital structure was appropriate and rejected PPLICA's alternative proposal. R.D., p. 159. PPLICA excepts to this recommendation.

The ALJ has approved a capital structure that is based on conjecture and speculation. During the evidentiary phase of the hearing, PP&L neither committed to the August equity issuance upon which its capital structure was based nor provided evidence of any numerical study evaluating whether the issuance would be a prudent financing effort. Tr. at 53-55. This Commission has ruled that where a proposed capital structure is based upon a possible issuance of equity, it must be denied as being too speculative. See Pennsylvania Public Utility Commission, et al, v. National Fuel Gas Distribution Corp., et al., 73 PaPUC 552, 605-06 (1990). As such, the ALJ's approval of PP&L's speculative capital structure is in error. PPLICA's proposal to utilize PP&L's actual September 30, 1994, capital structure (PPLICA Statement No. 8, p. 37) should be approved as it is the only reasonable alternative.

5. The ALJ Erred in Approving PP&L's Proposal to Levelize Its Modified Sinking Fund Depreciation for Its Susquehanna Units.

PP&L proposed to change the manner in which it accrued depreciation on its two nuclear units at the Susquehanna Steam Electric Station ("SSES") by switching from the modified sinking fund ("MSF") depreciation method to a levelized depreciation method. This proposed modification increased PP&L's test year expenses by approximately \$30 million. PP&L Statement No. 4, p. 13; PPLICA Statement No. 9, p. 16. The OTS, OCA and PPLICA opposed PP&L's proposed adjustment. See R.D., pp. 109-14. The ALJ recommended that the PP&L proposal be accepted by the Commission. Id. at 115. PPLICA excepts to this recommendation.

As PPLICA noted in its Main Brief (PPLICA Main Brief, pp. 40-41) and its Reply Brief (pp. 39-40), PP&L's proposal constitutes an attempt to reach beyond the end of the test year to examine a projected cost increase without accounting for potentially offsetting cost reductions or revenue increases. PPLICA Main Brief, p. 40. Likewise, the proposal fails to include an offsetting carrying charge benefit to levelize the effect of the increase (resulting from the change in methodology) on current ratepayers. Id. In addition, the Company's assertion that a rejection of its proposal would cause the Company to over-recover when its SSES depreciation expenses reduced to straight-line levels commencing in January 1999 under MSF depreciation is unreasonably speculative and not supported by the substantial record evidence. Id. at 41.

Furthermore, the bottom line is that the Commission approved the modified sinking fund method which PP&L (and the ALJ) now proposes to change because that depreciation methodology matched the economic benefits of the plant over its life cycle to the ratepayers. As recognized by PP&L Witness Hoch, the use of the modified sinking fund treatment maintains rate stability by not increasing rates beyond what they might reasonably be expected to be. Tr. at 117. Consequently, acceptance of the Company's proposal will increase the revenue requirement for ratepayers in contravention to the express rationale upon which the modified sinking fund treatment was approved in the first instance. Pennsylvania Public Utility Commission v. Pennsylvania Power & Light Company, 59 PaPUC 332 (1985). As such, the ALJ's recommendation should be reversed, and PP&L's requested revenue requirement should be reduced by \$30.626 million. See PPLICA Statement No. 9, p. 5; PPLICA Reply Brief, p. 41.³

³PPLICA's Main Brief p. 41 improperly identified the reduction to the revenue requirement as \$19.927. The citation in the Main Brief to PPLICA Statement No. 9, p. 5 correctly identifies the reduction to the revenue requirement as \$30.626 million. This was clarified in PPLICA's Reply Brief at p. 41, n. 4.

6. The ALJ Erred In Approving PP&L's Proposal To Increase Its Allowed Annual Nuclear Decommissioning Annuity.

PP&L requested an increase to its allowed annual nuclear decommissioning accrual for its Susquehanna Units, resulting in an increase to its revenue requirement of nearly \$20 million. The Company's proposal assumed an after tax rate of return on its nuclear trust fund of only 5.50%. PPLICA Statement No. 9, pp. 19-20, PPLICA Main Brief, p. 42. Both the OCA and PPLICA challenged PP&L's proposed rate of return on its nuclear trust fund. See R.D., pp. 86, 90. Despite noting that PP&L could well do better than a 5.5% return on its trust fund, the ALJ recommended retention of the 5.5% factor. Id. at 99. PPLICA excepts to this recommendation.

As per its Main and Reply Briefs, PPLICA believes that the Company should be required to manage its trust fund investments at a level comparable to that which it manages its rate base investments. Otherwise, PP&L will have no direct incentive to manage the trust fund aggressively on behalf of the ratepayers. PPLICA Main Brief, p. 42. As PPLICA stated in its in Reply Brief "[t]he bottom line is that PP&L wants ratepayer dollars far in advance of the date for decommissioning SSES, and ratepayers are entrusting PP&L with their money for a significant period of time." PPLICA Reply Brief, p. 35. PP&L ratepayers deserve a performance on their "investment" which is comparable to that which the ALJ has entitled PP&L to earn on its investment. As such, PP&L's annual SSES nuclear

decommissioning accrual should be adjusted to recognize a rate of return on its trust fund of 9.26% (the rate of return recommended by the ALJ for PP&L's investment).

**7. The ALJ Erred in Approving the Company's Proposal to
Defer an Amortized Cost Associated with its Voluntary Early
Retirement Program Without Adjustment.**

PP&L requested recovery of approximately \$76 million amortized over a five-year period for the cost of its Voluntary Early Retirement Program ("VERP"). PPLICA argued that the Company's proposal must be adjusted in two specific ways. First, the Company should be required to reduce the total cost of its VERP program by the amount of savings that it would have obtained by the end of the test year, and second, PPLICA proposed that recovery of its VERP costs should be amortized over a ten (10) year period, consistent with the length of PP&L's VERP plan. PPLICA Main Brief, pp. 43-44; PPLICA Reply Brief, pp. 30-32. The ALJ recommended adoption of the PP&L proposal and rejection of the alternatives proposed by PPLICA. R.D., p. 45. PPLICA excepts to this recommendation.

With respect to PPLICA's request that the total cost of the Company's VERP program be reduced by the amount of savings which it will have obtained by the end of the test year as a result of the program, the ALJ noted that he did "not discern evidence of cost decreases sufficient to justify the proposed adjustment." R.D., p. 44. As PPLICA noted in its Main Brief, the Company has achieved savings as a result of its program, and to allow the Company to recover the gross costs of the VERP despite the fact that the Company was the direct beneficiary of nine months of VERP related savings from the implementation of its plan beginning December 31, 1994, through September 30, 1995, is not justified on the record. PPLICA Main Brief, p. 43-44. Moreover, the ALJ did not "discern evidence" of

cost decreases in part because PP&L was not forthcoming in responding to an On-The-Record Data Request propounded by the OCA on this issue. OCA Main Brief, p. 159, n. 42; see PPLICA Reply Brief, pp. 31-32. As such, PP&L did not bear its burden of proof with respect to this issue, and the adjustment proposed by PPLICA regarding an offset for VERP savings should be incorporated, thereby reducing the Company's revenue requirement by approximately \$5 million. See PPLICA Statement No. 9, p. 28; PPLICA Main Brief, p. 44.

With respect to PPLICA's proposal to extend the amortization period for recovery of VERP costs, the ALJ based his rejection of that proposal on his assessment that "there is no return allowed on the amortizations and I would not string out the cost recovery to be allowed PP&L. . . . [A] five year period is more consistent with past practice and with the facts than would be a ten year period." R.D., pp. 44-45. In so doing, the ALJ unreasonably disregards the PPLICA argument that a ten-year straight-line amortization period for net VERP costs is more equitable than a five-year period since it more closely parallels the length of time during which actual payment will be made under the VERP. PPLICA Main Brief, p. 44; PPLICA Statement No. 9, pp. 28-29. In short, because the VERP expense is paid out and incurred over a ten-year period, recovery over a ten-year period of that expense is reasonable. PPLICA Reply Brief, p. 32. As such, the ALJ's recommendation should be reversed and the Company's revenue requirement should be reduced by an additional \$4 million to recognize an extension of the amortization period from

five to ten years for recovery of VERP costs. PPLICA Main Brief, p. 44; PPLICA Statement No. 9, p. 29.

8. The ALJ Erred in Approving PP&L's Proposal to Recover Costs Associated with Implementation of SFAS 106.

PP&L requested additional revenue of \$1.894 million to recover (over seventeen (17) years) the incremental costs associated with complying with Statement of Financial Accounting Standard No. 106 ("SFAS 106"). The OTS, OCA and PPLICA opposed this adjustment. R.D., p. 45. Based upon his conclusion that the SFAS 106 change was an extraordinary, non-recurring event, the ALJ recommended approval of PP&L's SFAS 106 cost recovery proposal. R.D., p. 50. PPLICA excepts to this recommendation.

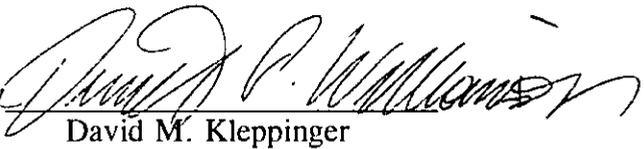
Given that the legality of SFAS 106 cost recovery is currently pending before the Courts of this Commonwealth, PPLICA believes that the PP&L proposal must currently be rejected. See PPLICA Reply Brief, pp. 32-34. Such a denial is consistent with this Commission's rejection of a similar claim by the West Penn Power Company in Pennsylvania Public Utility Commission v. West Penn Power Company, Docket No. R-00942986 Opinion and Order entered December 29, 1994. PP&L's expenses must be properly adjusted downward by \$1.797 million. PPLICA Statement No. 9, p. 5; PPLICA Main Brief, Appendix F, Table 2.

III. CONCLUSION

WHEREFORE, the PP&L Industrial Customer Alliance respectfully requests that this Commission grant the Exceptions set forth herein.

Respectfully submitted,

McNEES, WALLACE & NURICK

By 

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Dated: August 14, 1995

CERTIFICATE OF SERVICE

I hereby certify that I have served two copies of the foregoing document, the Exceptions of the PP&L Industrial Customer Alliance, on all known parties of record to this proceeding, in the manner indicated below, property addressed as follows:

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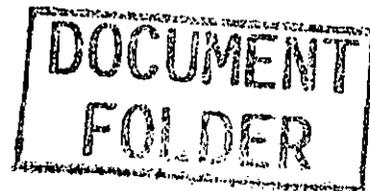
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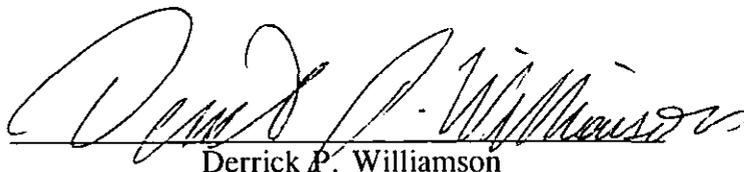
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Derrick P. Williamson

Dated this 14th day of August, 1995, in Harrisburg, Pennsylvania.

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF SMALL BUSINESS ADVOCATE

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Bernard A. Ryan, Jr.
Small Business Advocate

August 14, 1995

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John G. Alford, Secretary
Pa. Public Utility Commission
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Re: Pennsylvania Public Utility Commission v.
Pennsylvania Power & Light Company
Docket No. R-943271

Dear Secretary Alford:

Enclosed for filing are the original and nine (9) copies of the Exceptions of the Office of Small Business Advocate in the above-docketed proceeding. As evidenced by the enclosed certificate of service, copies have been served on all active parties in this case.

If you have any questions, please do not hesitate to contact me.

Sincerely,

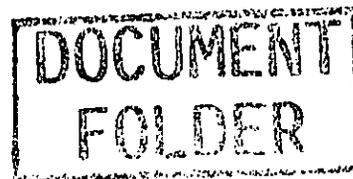
Karen Oill Moury
Assistant Small Business Advocate

Enclosures

cc: Cheryl W. Davis, Director
Office of Special Assistants
(2 copies with disk)

Hon. Robert A. Christianson
Administrative Law Judge

Parties of Record



ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY
COMMISSION

v.

PENNSYLVANIA POWER & LIGHT
COMPANY

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Docket No. R-943271

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EXCEPTIONS
OF THE
OFFICE OF SMALL BUSINESS ADVOCATE

DOCKETED
AUG 15 1995

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Dated: August 14, 1995

DOCUMENT
FOLDER

ORIGINAL

I. INTRODUCTION

On December 30, 1994, Pennsylvania Power & Light Company ("PP&L" or "Company") filed Supplement No. 50 to Tariff Electric-Pa. P.U.C. No. 200 to become effective for electric service rendered on and after February 28, 1995. By that filing, PP&L sought to increase its rate revenues by \$257,925,888, or 11.7%. Pursuant to the Commission's order entered on January 27, 1995, that filing was suspended and hearings were held to determine the lawfulness, justness and reasonableness of the Company's proposed and existing rates.

On July 31, 1995, the Office of Administrative Law Judge issued the Recommended Decision of Administrative Law Judge ("ALJ") Robert A. Christianson, providing for a revenue increase of \$61,744,000, or 2.6%. Pursuant to the cover letter of Acting Chief ALJ Christianson, exceptions of the parties are due on August 14, 1995, with replies due on August 21, 1995. In accordance with that directive, the Office of Small Business Advocate ("OSBA") hereby files Exceptions to ALJ Christianson's Recommended Decision ("R.D.").

Consistent with the positions advanced by OSBA during this proceeding to date, these Exceptions will address issues relating only to rate structure which is the subject of Section IX of the Recommended Decision. More particularly, these Exceptions will be limited to a discussion of the appropriate scaleback method to be employed in this case, in accordance with the ALJ's comments at pages 224-227 of the decision.

II. EXCEPTIONS

In his Recommended Decision, ALJ Christianson concluded that PP&L's proposed revenue allocation should be approved. R.D. at 226. Overall, the OSBA believes that the ALJ's recommendation on that issue is fair and equitable to PP&L's small business customers. Since the Company's proposed revenue distribution had provided for below system average increases to the GS-1 and GS-3 classes, in recognition of the high rates of return exhibited by those classes, adoption of the ALJ's recommendation will allow the rates for small businesses to begin moving toward cost of service.

In order to implement a lower revenue award than originally sought by the Company, the ALJ favorably discussed the OSBA's proposal for a weighted scaleback method, which is described in the OSBA's Main Brief at 22-28. See also OSBA Stmt. No. 1 at 7-12 and OSBA Stmt. No. R1 at 28-36. Specifically, ALJ Christianson indicated:

To the degree reasonably possible and feasible, I recommend that the Commission adopt the OSBA approach to a rate reduction (or very small increase) situation. I suggest that the OSBA and the other parties respond to this recommendation in their exceptions and reply exceptions.

R.D. at 227. Further, for any increase below that sought by the Company, the ALJ recommended that "some attempt be made to move more toward the overall rate of return, for the various classes, than would be the case under a straight scaleback approach." R.D. at 226.

The OSBA submits that the jurisdictional rate increase recommended by ALJ Christianson of \$61.744 million is a relatively

small increase of roughly 2.6%. More importantly, the suggested 2.6% increase is substantially lower than PP&L's proposed increase of 11.7%, for which PP&L's revenue allocation proposal was developed. Thus, the ALJ's conclusions relating to use of the weighted scaleback approach presented by the OSBA are applicable to his recommended level of rate relief.

To the extent that the ALJ's recommendation for adoption of the weighted scaleback approach is applicable to the level of relief ultimately awarded by the Commission, the OSBA's Exceptions do not challenge the ALJ's decision. Rather, these Exceptions specifically respond to the ALJ's request for guidance as to the impact of the weighted scaleback approach on the various customer classes at a relatively low revenue award. As the ALJ recognized, the combination of (1) a substantial reduction in the Company's revenue deficiency, and (2) the implementation of a simple proportional scaleback, would result in the lack of any measurable progress toward cost-based rates for PP&L's various customer classes. R.D. at 225. While the Company's proposed revenue distribution provides for a reasonable amount of movement by the small business classes (Rate Schedules GS-1 and GS-3) toward cost-based rates, a proportional scaleback to reflect the ALJ's recommended level of rate relief would simply not produce similar results. See OSBA M.B. at 19-22.

The OSBA's only Exception to the Recommended Decision relates to the ALJ's general suggestion for use of "a traditional scaleback approach if the overall increase is below the one

sought." R.D. at 226. Despite the ALJ's recommended adoption of the OSBA's weighted scaleback approach for a very small increase, and his remark that some attempt be made to improve upon a straight scaleback at any level of increase, he refrained from directing the Company to utilize the weighted scaleback approach to implement a higher revenue award. R.D. at 226.

Although the ALJ was persuaded by the OSBA's proposal for an alternative to a straight scaleback, he seemed to be concerned about the potentially skewed results that may occur for various classes if the weighted scaleback approach is implemented at any level of rate relief. While the ALJ's apprehension is understandable, the OSBA's witness, Robert D. Knecht, has provided the results of the weighted scaleback approach at varying levels of rate relief, none of which exhibit unusual increases for any particular customer class. See OSBA Exhibit 4. Thus, the ALJ's concern is unfounded and need not interfere with utilization of the weighted scaleback method.

The OSBA's Main Brief contains a thorough discussion of the weighted scaleback approach. OSBA M.B. at 23-28. As described, it includes a consideration of the increases that would result from both a proportional scaleback and a constant differential scaleback¹, and then produces increases that reflect a weighted average of these two methods. Under the weighted scaleback

¹ *The constant differential method is described in the OSBA's Main Brief at 22-23, with reference to OSBA Stmt. No. 1 at 9. Under that approach, the difference between the class increase and the system increase in the approved revenue allocation is maintained at whatever increase is ultimately adopted.*

approach, the relative weightings of the two different methods would depend upon the magnitude of the final increase. See OSBA Stmt. No. 1 at 11; OSBA Stmt. No. R1 at 30-32. In the case of an increase on the order of the ALJ's recommendation, substantially more weight (75%) is afforded the results of a proportional scaleback, with less weight (25%) being given to the results of the constant differential scaleback. Essentially, the weighted scaleback approach would retain more of the progress toward cost-based rates that was inherent in the Company's original proposal than would the proportional scaleback method.² See OSBA Stmt. No. 1 at 9.

In response to the ALJ's request for details of the impact that the OSBA's weighted scaleback approach would have on various customer classes, the OSBA submits Appendix A. This table shows the actual dollar and percentage increases that would result from a proportional scaleback, a constant differential scaleback and a weighted scaleback at the ALJ's recommended revenue deficiency of \$61.744 million. The data supplied in Appendix A was developed using the method and formulae thoroughly described in Mr. Knecht's direct and rebuttal testimony. See OSBA Stmt. No. 1 at 11-12 and OSBA Exhibit 4; OSBA Stmt. No. R1 at 30-32. We note that in OSBA Exhibit 4 accompanying his direct testimony (OSBA Stmt. No. 1), Mr. Knecht furnishes the same information for hypothetical revenue deficiencies of \$64.5 million, \$129 million and \$193.5 million.

² As explained by the OSBA's witness, "the constant differential method produces progress toward cost-based rates that is more similar to the original proposal than the proportional scaleback approach." OSBA Stmt. No. 1 at 9.

As shown on Appendix A, a \$61.744 million revenue deficiency would result in an increase of 3.4% to the Residential class if a proportional scaleback method is employed. The constant differential approach would result in a 6.1% increase to the Residential class. If, however, the weighted scaleback method is used, the Residential class increase would be 4.1%. Similarly, the GS-3 class would be increased by 1.5% under a proportional scaleback, reduced by 2.4% using a constant differential method, and increased by .5% if a weighted scaleback is implemented.

The only decrease that would occur using the weighted scaleback approach for the ALJ's recommended revenue deficiency would be a minimal reduction of .7% in the GS-1 revenues. In view of PP&L's cost of service study results (PP&L Exhibit OGK-3), which show that class as contributing almost twice the system average return at present rates, and the ALJ's rejection of the OSBA's proposal for an annual automatic adjustment mechanism for this class (R.D. at 261), the OSBA believes that a modest decrease in rates for the GS-1 class in the context of an overall system revenue increase of 2.6% is justifiable on sound ratemaking principles.

With respect to higher revenue deficiencies than recommended by the ALJ, OSBA Exhibit 4 sheds some light on the potential results of implementing a weighted scaleback approach. For example, if the Commission were to award PP&L one-half of its requested revenue increase, the Residential increase would be 7.6% using a proportional scaleback, but would be 8.5% if a weighted

scaleback is employed. By contrast, the GS-3 class, which would be increased by 3.4% under a proportional scaleback, would experience a 2.1% increase using a weighted scaleback. At this level of rate relief, the GS-1 rates would increase by 1.9% if PP&L's proposal is proportionally scaled back, but would remain unchanged if a weighted scaleback approach is employed.

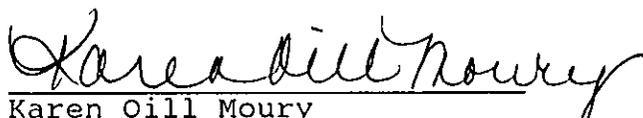
Although the weighted scaleback method is not ideal because it would not maintain the same level of progress toward cost-based rates that was inherent in the Company's original proposal, it is superior to a proportional scaleback in that it would at least preserve some level of progress toward that goal. Clearly, ALJ Christianson agreed that regardless of the final revenue award in this case, major classes of customers should move toward the system average rate of return. R.D. at 224.

While the OSBA obviously cannot provide the Commission with information showing the exact consequences of the weighted scaleback approach at every possible level of rate relief in this case, we have furnished numerous examples of the effects of that method at varying levels of rate relief. Through those examples, the OSBA has established that the weighted scaleback approach would impose no unusual increases on any customer class. Therefore, the OSBA urges the Commission to rely upon the ALJ's rationale and discussion at pages 224-227 and direct PP&L to implement the weighted scaleback approach at whatever level of rate relief is finally awarded in this proceeding.

III. CONCLUSION

The Office of Small Business Advocate respectfully requests that the Commission grant these Exceptions and direct that Pennsylvania Power & Light Company utilize the weighted scaleback approach explained here and fully described in the OSBA's testimony and briefs to allocate any revenue increase approved in this case.

Respectfully submitted,


Karen Oill Moury
Assistant Small Business Advocate

Dated: August 14, 1995

APPENDIX A

OSBA PROPOSED DEFICIENCY ASSIGNMENT METHODS FOR PP&L -- ALJ DEFICIENCY

Class	PP&L PROPOSAL			\$61.744 MILLION DEFICIENCY <i>Class Deficiency Assignment</i>		
	Present Revenues (5)	Proposed Revenues (5)	Deficiency	Proportional Scaleback	Constant Differential	Weighted Scaleback
RS	887.11	1,022.73	135.62	30.50	54.37	36.47
RTS	19.77	23.21	3.44	0.77	1.63	0.99
GS-1	162.22	168.52	6.30	1.42	(8.55)	(1.08)
GS-3	507.17	541.27	34.10	7.67	(12.35)	2.66
LP-4	273.35	301.14	27.78	6.25	2.75	5.37
LP-5	259.61	299.72	40.11	9.02	16.33	10.85
LPEP	8.40	8.87	0.46	0.10	(0.31)	0.00
SL/AL	21.16	24.19	3.02	0.68	1.09	0.78
GH(R)	43.63	50.67	7.04	1.58	3.05	1.95
Sub-Total	2,182.43	2,440.32	257.89	57.99	57.99	57.99
ISA	20.45	20.48	0.03	0.03	0.03	0.03
Standby	1.15	1.16	0.01	0.01	0.01	0.01
Sub-Total	21.60	21.64	0.04	0.04	0.04	0.04
Rate Class Revs.	2,204.03	2,461.96	257.93	58.03	58.03	58.03
Other Revs./Adj. (6)	198.22	201.94	3.71	3.71	3.71	3.71
Jurisdiction Revs.	2,402.26	2,663.89	261.64	61.74	61.74	61.74
<i>Percent Change in Rates</i>						
RS	887.1	1,022.7	15.3%	3.4%	6.1%	4.1%
RTS	19.8	23.2	17.4%	3.9%	8.2%	5.0%
GS-1	162.2	168.5	3.9%	0.9%	-5.3%	-0.7%
GS-3	507.2	541.3	6.7%	1.5%	-2.4%	0.5%
LP-4	273.4	301.1	10.2%	2.3%	1.0%	2.0%
LP-5	259.6	299.7	15.4%	3.5%	6.3%	4.2%
LPEP	8.4	8.9	5.5%	1.2%	-3.7%	0.0%
SL/AL	21.2	24.2	14.3%	3.2%	5.1%	3.7%
GH(R)	43.6	50.7	16.1%	3.6%	7.0%	4.5%
Sub-Total	2,182.4	2,440.3	11.8%	2.7%	2.7%	2.7%
ISA	20.4	20.5	0.2%	0.2%	0.2%	0.2%
Standby	1.1	1.2	0.7%	0.7%	0.7%	0.7%
Sub-Total	21.6	21.6	0.2%	0.2%	0.2%	0.2%
Rate Class Revs.	2,204.0	2,462.0	11.7%	2.6%	2.6%	2.6%
Other Revs./Adj. (6)	198.2	201.9	1.9%	1.9%	1.9%	1.9%
Jurisdiction Revs.	2,402.3	2,663.9	10.9%	2.6%	2.6%	2.6%

Notes:

- 1) Proportional Scaleback: Original class deficiency is reduced by the percentage decline in the overall deficiency.
- 2) Constant Differential: PP&L class proposed percent increase in rates is reduced by the differential between the PP&L system percent increase and the revised system increase.
- 3) Weighted Scaleback: $w * (\text{proportional scaleback deficiency}) + (1-w) * (\text{constant differential deficiency})$, where $w = 1 - (\text{revised deficiency}) / (\text{original deficiency})$; $w \leq 75\%$.
- 4) ISA and Standby classes are assumed to exhibit no change in the proposed deficiency.
- 5) Source: Exhibit Future I, D-3
- 6) Source: Exhibit JMK-2

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY
COMMISSION

v.

PENNSYLVANIA POWER & LIGHT COMPANY :

Docket No. R-94321

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CERTIFICATE OF SERVICE

I certify that I am today serving copies of the exceptions on behalf of the Office of Small Business Advocate in the manner indicated upon the persons addressed below:

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August 14, 1995

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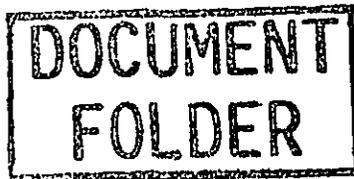
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Re: Pennsylvania Public Utility Commission, et al. v.
Pennsylvania Power and Light Company,
Docket No. R-00943271 et seq.

Dear Mr. Alford:

Enclosed for filing are an original and nine (9) copies of the Exceptions of the University/College Coalition in this matter. One copy is being served on all active parties of record in the manner indicated on the attached Certificate of Service.

Respectfully submitted,



James P. Melia
James P. Melia

JPM/pkw
Enclosure

cc: Parties of Record per
Certificate of Service (w/encl.)

ORIGINAL

BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION
ADMINISTRATIVE LAW JUDGE ROBERT A. CHRISTIANSON PRESIDING

PENNSYLVANIA PUBLIC UTILITY
COMMISSION, et al.

v.

PENNSYLVANIA POWER AND LIGHT
COMPANY.

Docket No. R-00943271

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EXCEPTIONS OF
UNIVERSITY/COLLEGE COALITION

Exceptions to the Recommended Decision of
Administrative Law Judge Robert Christianson
Filed Pursuant to Section 5.533
of the Commission's Regulations,
52 Pa. Code § 5.533.

Daniel P. Delaney
James P. Melia

Counsel for University/
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Dated: August 14, 1995

DOCKETED

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ORIGINAL

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STATEMENT OF THE CASE

On December 30, 1994, Pennsylvania Power and Light Company ("PP&L") filed its Supplement No. 50 to Tariff Electric-Pa. P.U.C. No. 200, proposed to become effective February 28, 1995. In its filing, PP&L requested a \$261 million or 11.7% increase in its annual electric base rate revenues. On or about February 23, 1995, the Pennsylvania Public Utility Commission ("Commission") suspended Supplement No. 50 pursuant to Section 1308(d) of the Public Utility Code ("Code"), 66 Pa. C.S. § 1308(d), and initiated an investigation into the lawfulness, justness and reasonableness of the rates, rules and regulations proposed in those tariff supplements. The investigation was assigned initially to Administrative Law Judge ("ALJ") Michael C. Schnierle and then to Robert A. Christianson as Presiding Officer.

On March 6, 1995, a Petition to Intervene was filed by the University/College Coalition ("UCC"), an ad hoc coalition of colleges and universities in the PP&L service territory. For purposes of this proceeding, the UCC consists of Muhlenberg College, Wilkes College, Kings College, Messiah College, University of Scranton, Elizabethtown College, Dickinson College and Keystone Junior College. The UCC, in its Petition, averred that its members predominantly receive service under PP&L's existing Rate Schedules LP-4 and GS-3 and various riders and related tariffs. The Petition further alleged that the cost of electric utility service is a significant component in UCC

members' cost of operation and that the proposed rate increase and tariff changes may have an adverse impact on UCC members.

A Prehearing Conference in this case was held on March 7, 1995 and UCC's Petition to Intervene was granted. Approximately 15 days of hearings were conducted in this proceeding. The record closed in this matter on May 26, 1995.

UCC presented the Direct and Surrebuttal Testimony and supporting exhibits of Kenneth Eisdorfer. (UCC St. Nos. 1 and 2). Mr. Eisdorfer presented testimony on the issues of cost of service and interclass subsidization. UCC also cross-examined other parties' witnesses concerning their positions on cost of service issues.

UCC filed its Main and Reply Briefs in a timely manner. ALJ Christianson issued his Recommended Decision in this matter on July 31, 1995. These Exceptions are being filed in response to that Recommended Decision.

The UCC believes that ALJ Christianson has produced a comprehensive decision which attempts to balance the interests of all parties to this proceeding. Although UCC submits that ALJ Christianson's Recommended Decision correctly decides many difficult issues in this case, UCC files these Exceptions to several determinations for purposes of requesting the Commission to modify those determinations in its Final Order. As detailed below, ALJ Christianson failed to adopt several of the recommendations advanced by UCC witness Kenneth Eisdorfer in his Direct Testimony (UCC St. No. 1). The UCC respectfully requests

the Commission adopt these proposed modifications to ALJ
Christianson's Recommended Decision in its Final Order in this
matter.

EXCEPTIONS

I. **ALJ CHRISTIANSON'S RECOMMENDATION REGARDING ADOPTION OF THE 12 CP COST OF SERVICE METHOD SHOULD BE REJECTED.**

ALJ Christianson adopts PP&L's recommendation regarding use of the monthly peak demand responsibility allocation methodology ("12 CP method") at pages 203 through 205 of his Recommended Decision. The 12 CP method allocates generating and transmission plant costs based on the average of the 12 monthly coincident class demands at the time of the system monthly peak loads. The 12 CP method, according to PP&L, recognizes that generating costs are incurred to meet peak demand requirements and also recognizes that these demand requirements continue throughout the year. PP&L further supports use of the 12 CP method at pages 233-234 of its Main Brief.

In contrast, the UCC, through the Direct Testimony of its witness, Kenneth Eisdorfer (UCC St. No. 1, Exhibit KE-1) advocated reliance upon the single peak or 1 CP methodology. The UCC has thoroughly addressed the substance of Mr. Eisdorfer's position in support of the 1 CP method at pages 4 through 19 of its Main Brief. The 1 CP methodology allocates production and transmission capacity costs based on the annual system peak. In PP&L's case, that peak invariably occurs in the winter months. (UCC St. No. 1, p. 5). PP&L likewise considers the annual system peak (i.e., winter peak) to be predominant with respect to its capacity resource planning as testified to by its own witness, Mr. Sipics (PP&L St. No. 9, p. 5; Ex. JFS-1). Mr. Eisdorfer

concluded, based on a detailed analysis of PP&L system capacity requirements, that PP&L considers the size of its annual system peak to be the driving force with respect to the amount of capacity it must have available for its customers. (UCC St. No. 1, p. 5).

Despite clear and convincing evidence put forward by UCC witness Eisdorfer, regarding adoption of the 1 CP methodology, ALJ Christianson recommended adherence to PP&L's 12 CP method, apparently swayed by PP&L arguments regarding the usage levels relative to available capacity that place strenuous demands on the system in off-peak months due to heavy scheduled maintenance in such off-peak periods. ALJ Christianson also found convincing PP&L's arguments regarding the 12 CP method's contribution to rate stability. (Recommended Decision, pp. 204-205). Further, the ALJ implicitly appears to adopt the 12 CP methodology because, as several parties point out, that is the way that it has been done previously.

The fact that the 12 CP may have proven adequate in the past should not preclude this Commission from consideration of other equally valid cost of service methodologies which find clear support in the record and accurately reflect cost of service responsibility. The 1 CP method is, as many parties concede, just such a method.

Further, ALJ Christianson concedes that the winter peak approach "has considerable appeal and is, in my view, the classic approach". (Recommended Decision, p. 204). ALJ Christianson

recognizes that adoption of the 1 CP methodology would make demand charges depend on the largest peak of the year during the winter, the maximum service season for PP&L. The Commission should thus give additional consideration to the 1 CP methodology advocated by UCC and not adopt a "lock-step approach" toward the 12 CP method as has been done in the past.

UCC would recommend the Commission closely review the detailed empirical analysis put forward by Mr. Eisdorfer in his Direct and Rebuttal Testimony and associated exhibits. (UCC St. Nos. 1, 2; Exhibits KE-1, 2). The inescapable conclusions reached in that testimony are as follows:

1. PP&L considers the annual system peak (i.e., the winter peak) to be predominant with respect to capacity resource planning as supported by its own witness, Mr. Sipics. (PP&L St. No. 9, p. 5; Ex. JFS-1).

2. PP&L's annual system peak invariably occurs in the winter months. (UCC St. No. 1, p. 5).

3. The coincident peak to be employed, for allocation of demand-related production and transmission costs, is the annual system peak (i.e. the winter peak). (UCC St. No. 1, pp. 5-6).

4. The 12 CP method incorporates nine months that have never contained the annual system peak and have virtually no chance to do so in the future. (UCC St. No. 1, p. 7).

5. The loads for the remaining nine months outside of the winter peak period are not determinants of the amount of PP&L's

bulk power capacity and should not be relied on for assigning cost responsibility to customer classes. (UCC St. No. 1, pp. 7-8).

6. The 12 CP method is inconsistent with the determination of PP&L's installed capacity obligation ("ICO") to the PJM interchange. In fact, PP&L's winter peak is the overwhelming determinant of its ICO. (UCC St. No. 1, p. 8).

7. The role of the remaining nine months in determination of PP&L's ICO is insignificant. (UCC St. No. 2, p. 5).

The UCC herein incorporates its detailed arguments appearing at pages 5-8 of its Main Brief as well as the Testimony and Exhibits of Mr. Eisdorfer cited previously.

Other parties to this proceeding also disagree with PP&L's reliance on the 12 CP methodology employed by PP&L. PP&L Industrial Customer Alliance ("PPLICA") witness Stephen J. Baron testified that a single coincident-peak methodology, based on the winter peak of PP&L during the test year, should be the basis for allocating costs to the customer classes. Mr. Baron also critiqued PP&L's alleged justifications for reliance on the 12 CP method. (PPLICA St. No. 7, p. 18). Despite his support for the 1 CP method, Mr. Baron utilized the 12 CP method in his recommendations based on the Commission's prior adoption of the method in the last rate case. (PPLICA St. No. 7, p. 19).

Further, Bethlehem Steel witness Brubaker criticized PP&L's reliance on the 12 CP method contending that PP&L's predominantly

winter peaking characteristics make a winter peak cost of service study more appropriate. Mr. Brubaker, however, adopted PP&L's 12 CP study for purposes of his analysis although he does not view it as the most appropriate method. (Bethlehem Steel St. No. 1, p. 8).

Thus, it appears that the prevailing reason for adoption of the 12 CP method by the ALJ and by many of the parties is that "it has always been done that way" without recognition of the inherent deficiencies in the 12 CP method as applied to PP&L. The UCC recommends the Commission closely examine the evidence put forth by UCC witness Mr. Eisdorfer in his testimony and exhibits and give further consideration to adopting the 1 CP method.

The ALJ's reliance on PP&L's arguments regarding the impact of off-peak scheduled maintenance on its available capacity also lacks support in the record. (Recommended Decision, pp. 204-205). UCC effectively rebutted PP&L's assertion that the 12 CP method recognizes the impact of scheduled maintenance on capacity requirements. UCC also addresses these issues at pages 17 through 19. Through the Rebuttal Testimony of its witness Mr. Kleha, PP&L contended that the 1 CP method ignores customer-imposed demands on PP&L's system every month of the year and fails to recognize that calculation of PP&L's ICO is based on the provision of levelized amounts of capacity for the entire 12 months of each year. (PP&L St. No. 7-R, p. 6). Further, PP&L contended that its maximum capacity requirements (monthly peak

load plus scheduled maintenance requirement) do not always occur in the three month winter period of December through February. (PP&L St. No. 7-R, pp. 6-7).

In surrebuttal, UCC witness Mr. Eisdorfer criticized and effectively neutralized PP&L's arguments regarding justification of the 12 CP method based on the impact of scheduled maintenance outside of the winter peak period. Mr. Eisdorfer's analysis concluded that the timing of PP&L's scheduled maintenance is a function of the load characteristics of the utility and that utilities specifically schedule the bulk of their maintenance during months when there is no risk that winter extremes will create a capacity shortage problem. (UCC St. No. 1, p. 8).

Mr. Eisdorfer further observed that, for the period of 1992 through 1994, more than two-thirds of PP&L's capacity removed from service for scheduled maintenance occurred during the relatively "weather quiescent months" of March, April, May, October and November. These are months that have never contained the annual system peak and have no chance to do so in the future. Thus, the scheduling of generation maintenance has no impact on PP&L's cost causation for production plant which is driven by annual system peaks always occurring in the winter. (UCC St. No. 2, pp. 8-9).

Further, Mr. Eisdorfer demonstrated that the maximum capacity shown by PP&L differs from those derived by witness Eisdorfer. Mr. Eisdorfer's analysis demonstrated that the maximum capacity requirement occurs more in the winter peak

period than it does during spring or fall months. (UCC St. No. 2, p. 9; UCC Ex. KE-2, Schedule 2). Thus, ALJ Christianson unjustifiably relied on defective arguments advanced by PP&L regarding the effect of off-peak scheduled plant maintenance on capacity requirements in his selection of the 12 CP method.

II. THE ALJ ERRED IN FAILING TO ADOPT MR. EISDORFER'S RECOMMENDATIONS TO REDUCE INTERCLASS SUBSIDIZATIONS.

At pages 224 through 227 of the Recommended Decision, ALJ Christianson appears to adopt PP&L's proposal on revenue distribution implicitly rejecting the revenue distribution recommendations and concerns over interclass subsidizations raised by other parties. It must be recognized, however, that the ALJ appreciates the existence of the interclass subsidization problem but believes it cannot be adequately dealt with in the context of this case. The ALJ errs in failing to address existing interclass subsidizations and the perpetuation of such subsidies in PP&L's rate filing.

UCC's arguments regarding the existence of and remedies for existing severe interclass subsidization appear at pages 19 through 28 of its Main Brief. Mr. Eisdorfer calculated that the current subsidy provided by four rate classes, GS-1, GS-3, LP-4 and LP-5 currently totals \$227.5 million per year. This severe interclass rate subsidy is further illustrated in an excerpt from UCC St. No. 1 prepared by Mr. Eisdorfer at Table 2, page 9 of the Direct Testimony and reproduced at page 20 of UCC Main Brief:

Table 2

<u>Rate Class</u>	<u>Present Revenue (000)</u>	<u>Subsidy Provided (000)</u>	<u>Percent</u>
GS-1	\$ 162,217	\$ 46,949	28.9%
GS-3	507,172	112,339	22.2
LP-4	273,353	52,803	19.3
LP-5	<u>259,612</u>	<u>15,385</u>	5.9
Total	\$1,202,354	\$ 227,467	18.9%

As Mr. Eisdorfer observed, this subsidy represents 88.2% of PP&L's requested jurisdictional rate increase. On average, Mr. Eisdorfer calculated that 18.9 cents of every dollar paid by these ratepayers is used to pay the cost of providing power to a subsidized customer. A vast majority of this subsidy or approximately \$219.6 million benefits residential customers to the detriment of the economic vitality of the service territory. (UCC St. No. 1, pp. 9-10).

PP&L attempts to justify its proposed class revenue distribution by examining changes in class rates of return as a percentage of the system rate of return at proposed rates as compared to those at present rates for the 12 CP cost of service study. Mr. Eisdorfer, however, conclusively demonstrated the inapplicability of examining changes in class rate of return to justify revenue distribution. (UCC Main Brief, pp. 21-23; UCC St. No. 1, pp. 10-11; Ex. KE-1, Schedule 2, pp. 1-2).

Mr. Eisdorfer then demonstrated that PP&L's proposed revenue distribution only exacerbates levels of interclass subsidies effectively moving rates away from costs, as compared to the current revenue distribution, for 64% of the customer classes. (UCC Main Brief, pp. 23-25; UCC St. No. 1, p. 13; Ex. KE-1, Schedule 4). PP&L's proposal therefore increases existing class subsidies for rate classes RS, LP-4 and LP-5. The dollar value associated with these subsidies also increases as is illustrated in UCC Exhibit KE-1, Schedule 5.

Mr. Eisdorfer further demonstrated the degree of subsidization that would exist on the PP&L system if PP&L's revenue distribution were to be implemented. The degree of subsidization, illustrated in the table that follows, is excerpted from Mr. Eisdorfer's Direct Testimony (UCC St. No. 1, p. 14 (Table 5)) and was also cited at page 24 of UCC's Main Brief:

<u>Rate Class</u>	<u>Return on Common Equity</u>
GS-1	29.97%
GS-3	27.31%
LP-4	30.60%
LP-5	24.83%

This calculation shows the rate of return on common equity that would be earned on service to PP&L's major commercial and industrial classes at proposed rates. It should be noted that these return on equity amounts are significantly greater than PP&L's claimed cost of equity of 13%. Obviously, the foregoing equity returns will be impacted if a lesser revenue level is ultimately adopted but the fundamental interclass subsidization problem will still exist if PP&L's proposed revenue distribution is adopted.

As a proposed remedy to the existing interclass subsidies, Mr. Eisdorfer recommended a number of steps be adopted to reduce the subsidy situation on PP&L's system. These recommendations are as follows:

1. Reduce subsidies that are currently being received by the subsidized classes by one-half with the constraint that no class incur an

increase that is more than three times the overall increase requested by PP&L for the jurisdiction of 11.7%.

2. Reduce the subsidies that are currently being paid by the subsidized classes by a uniform percentage.
3. The rate class increase to Rate ISA is limited by a special contract. Therefore, the revenue level for this class would be as proposed by PP&L.

(UCC St. No. 1, pp. 15-16).

The details regarding Mr. Eisdorfer's revenue distribution recommendation are further explained in detail at pages 26 and 27 of UCC's Main Brief. Further, the results of Mr. Eisdorfer's recommended class revenue distribution appear at Schedule 6 of Exhibit KE-1 appended to UCC's Main Brief. The resulting class rates of return and corresponding subsidies appear at Schedule 7 and 8 of Exhibit KE-1 appended to UCC's Main Brief.

Mr. Eisdorfer's revenue distribution proposal would move each of PP&L's major customer classes significantly closer towards cost and dramatically decrease the overall interclass subsidization that currently exists on PP&L's system. It should be noted that, even though the figures on Exhibit KE-1, Schedule 6 reflect PP&L's requested jurisdictional revenue increase, Mr. Eisdorfer is not endorsing the level of that request, nor has ALJ Christianson recommended that level. Adoption of Mr. Eisdorfer's revenue distribution recommendations would have to be reconciled

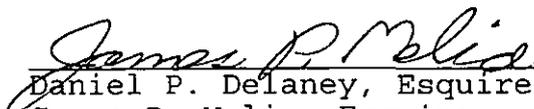
with whatever level of revenues is adopted by the Commission in this proceeding.

ALJ Christianson intimates that a lesser rate increase may present the appropriate opportunity to remedy the interclass subsidy problem. Based on the ALJ's revenue recommendation, this is just such an opportunity. With the infrequency of PP&L's base rate filings, such opportunities may prove few and far between.

CONCLUSION

For all the foregoing reasons, the University/College Coalition respectfully requests the Commission adopt the foregoing Exceptions to the Recommended Decision of ALJ Christianson in entering its Final Order in this matter.

Respectfully submitted,



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Counsel for University/
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Dated: August 14, 1995

BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION
ADMINISTRATIVE LAW JUDGE ROBERT CHRISTIANSON PRESIDING

PENNSYLVANIA PUBLIC UTILITY
COMMISSION, et al.

v.

PENNSYLVANIA POWER AND LIGHT
COMPANY

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:
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Docket No. R-00943271

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the Exceptions of the University/College Coalition upon the parties identified below in accordance with the requirements of Section 1.54 (relating to service by a participant).

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AUG 14 1995

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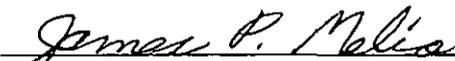
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MID-ATLANTIC ENERGY PROJECT

A Project of the Pace University School of Law
Center for Environmental Legal Studies

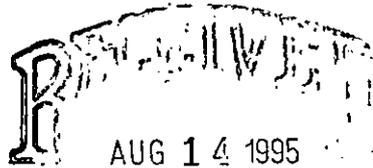
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August 14, 1995



John J. Alford, Secretary
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Room G-23, North Office Building
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Hand-delivered
SECRETARY'S OFFICE
Public Utility Commission

RE: Pennsylvania Public Utility Commission v. Pennsylvania Power & Light Co.,
Docket No. R-00943271
Exceptions of Sierra Club

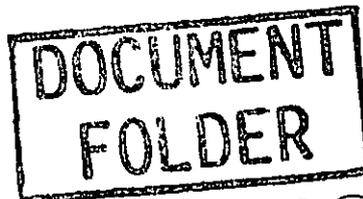
Dear Secretary Alford:

Enclosed please find enclosed the original and nine (9) copies of Exceptions of Sierra Club. All parties of record have been duly served as evidenced by the attached Certificate of Service. Since our attachments are the same as those provided with our Brief, we have omitted same from our mailing to the parties, and will provide another set if specifically requested.

Please return the enclosed copy of this transmittal letter, the Exceptions of Sierra Club and our Certificate of Service time-stamped for our files.

Very truly yours,

Alan J. Barak
Mid-Atlantic Energy Project
Attorney for Sierra Club



AJB/mlm
Enclosures

cc: Office of Special Assistants
Parties of Record

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COMMONWEALTH OF PENNSYLVANIA
BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility)
Commission)

v.)

Docket No. R-00943271

Pennsylvania Power & Light Co.)
(General rate increase request))

EXCEPTIONS OF SIERRA CLUB

DOCKETED

SUMMARY OF EXCEPTIONS

AUG 14 1995

EXCEPTION 1: THE ALJ SHOULD HAVE INCLUDED THE SIERRA CLUB DSM TESTIMONY AS RELEVANT TO SETTING PP&L RATES.

Sierra Club offered the expert testimony of Bruce Biewald of the Tellus Institute on the technical basis for, and design of, DSM incentives and lost revenue recovery. Per the Commonwealth Court's recent decision, a general rate case is the only forum in which to address incentives for DSM, and one of the two forums in which to address the basis for lost revenue recovery. The Sierra Club testimony responded directly to the Court's posturing of the DSM Order.

On motion, the ALJ excluded the Biewald DSM testimony. The ALJ denies Sierra Club's Brief's request for reconsideration and reaffirms his initial decision.¹ We recognize that, once having made the interlocutory ruling excluding the DSM testimony, the ALJ had no duty to further address the matter of certify it to the Commission for expedited review. Thus, these Exceptions are the appropriate place to seek the Commission's review of the DSM testimony exclusion.

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¹ Recommended Decision pp. 262-65, 275-76

We request that the Commission reverse, and remand within a limited phase of this docket the issues which the excluded testimony presents. This is fair, since principal parties to this case, PPLICA, PP&L, and the OCA opposed even the creation of a separate record at the time.

EXCEPTION 2: THE RD SHOULD HAVE RECOMMENDED FULL FUNDING OF ENVIRONMENTAL REMEDIATION BECAUSE CLEANING UP OR AVOIDING POLLUTION IS A COST OF PROVIDING POWER.

The Company sought a \$5.4 million adjustment (\$4.4 million jurisdictional) for environmental remediation. OTS opposed the figure as too high, and in excess of a \$5.0 million per year settlement with the DER (now the "DEP"). The ALJ adopted OTS' "modest" \$400,000 per year adjustment as tracking a DER settlement that took place during this case's litigation.² While the adjustment seems to track the settlement it provides the wrong signals to management, and may not track the realities of environmental cleanup costs.

As we did below, we recommend that the environmental remediation be treated as a fund for ratemaking purposes. If the Company's reasonable and prudent expense level is \$400,000 in excess of its settlement because the settlement is a floor, not a ceiling, on such expenditures, the Commission should not force the shareholders to cover legitimate costs engendered through service to the customers. A fund approach will ensure the expenditures go where intended, which appears to be part of OTS' concerns.

EXCEPTION 3: THE RD SHOULD HAVE RECOMMENDED TERMINATING THE COMPANY'S ECR IN ORDER TO FOSTER THE MOST ECONOMICALLY EFFICIENT PURCHASES OF ENERGY RESOURCES.

The Company case, of course, supported continuation of the ECR for fuel and power costs. Responding to PP&L's proposal to expand the use of the clause when some capacity reverts

² Recommended Decision pp. 64-65. Table II to the RD suggests that the ALJ scaled back his disallowance to a jurisdictional \$326,000.

to it, we urge the Commission to reject the further use of the clause as providing an unnecessary subsidy to fossil fuels at a time of fuel price stability and increasing competition. The ALJ supports continuation of the ECR, noting that it avoids more frequent rate proceedings and has appropriate checks, and recommends adoption of PP&L's alternative proposal for its JCP&L capacity return.³

There is no compelling reason to retain the ECR if the Commission is serious about posturing the Commonwealth's utilities for a more competitive environment. The ECR gives them an unfair advantage over other providers, and other sources, of energy. Indeed, by shielding the utility from cost pressure, and therefore cutting back on the frequency of general rate cases, as the ALJ recognized, the clause makes it harder for the Commission to keep track of the overall performance of Pennsylvania's utilities during these changing times.

At the very least, the ECR should be thrown into "the pot" of regulatory changes that the Commission considers in moving Pennsylvania toward more electric competition. Perhaps, in the alternative, the Commission should put PP&L on notice that the ECR may not survive until PP&L's next planned rate case. However, the more forthright action would be to eliminate the clause now, and propel PP&L management immediately toward the more exacting standards of resource procurement in a competitive environment.

EXCEPTION 4: THE RD FAILS TO RECOMMEND THAT CUSTOMER AND COMMUNITY NEEDS PROGRAMS BE ADEQUATELY FUNDED; THEY CONTRIBUTE BENEFITS TO THE PP&L SYSTEM.

PP&L has responded to the responsibilities attendant upon its unique market and life-sustaining position in the Commonwealth by proposing "social" programs that increase the affordability of electric service to its customers. OTS, primarily, opposes the programs on, *inter alia*, the theoretical ground that the programs are not part and parcel of service to the customers. With CEO and Sierra Club, among others, supporting such PP&L programs, and recommending augmentations, the ALJ rejects the OTS adjustments, "giving PP&L the

³ Recommended Decision pp. 268-73, citing PP&L Brief pp. 294-95 and PP&L St. 7-R, pp. 34-35 (Kleha).

benefit of the doubt" as to the ratemaking, as opposed to the social, utility of the programs.⁴ We except to the RD only to the extent that the ALJ failed to recommend CEO's enhancements and our suggested reporting mechanism.

EXCEPTION 5: THE RD FAILS TO PROVIDE THAT NUCLEAR DECOMMISSIONING EXPENSE BE INCREASED TO REFLECT FULLY THE COMPANY'S RECENT, CONSERVATIVE RE-ESTIMATES IN ORDER TO INSURE THAT THE MONEY IS AVAILABLE WHEN NEEDED.

While the ALJ agreed to accept PP&L's estimates of increased decommissioning costs for both "hot", or radiological, structures and the other, nonradiological structures, and its financing approach, he rejected the use of PP&L's engineer's contingency factor.⁵ While we share the ALJ's concerns that addressing uncertainty should not turn into "overkill"⁶, and we believe strongly in the shareholders taking responsibility for their management's selection of the nuclear energy resource, we must except on the ground that the PP&L estimate from Mr. LaGuardia has too many built in underestimates. The ALJ's carving out the contingency simply exacerbates the undercollection situation.

It is simply not in the Commonwealth's interest to underfund the treatment of radioactive poisons with lives of tens of thousands of years. Given the unlikelihood of PP&L's returning for a general rate case until the next century, and the absence of any other mechanism for collecting for nuclear decommissioning costs, this is the last opportunity for this Commission to adjust PP&L's nuclear decommissioning rates for some time.

⁴ Recommended Decision pp. 72-80, 80.

⁵ Recommended Decision pp. 81-99, 98-99.

⁶ Recommended Decision p. 99.

EXCEPTION 6: THE RD WOULD SEND THE WRONG PRICE SIGNALS TO CUSTOMERS BY SETTING THE CUSTOMER CHARGE TOO HIGH AND PERMITTING A THIRD BLOCK -- THE RS CHARGE SHOULD BE SET AT \$4.80.

PP&L would substantially raise the customer charge and offer discounts for increased usage through a declining block rate structure. We oppose the increase on the ground that it sends the wrong price signals to customers, and, given the changes likely in the electric utility industry until the next PP&L rate case, will constitute an anachronism of monopoly pricing. The ALJ rejects the parties' attacks on the PP&L proposal and recommends, without citation to record support, a 35% increase in the customer charge, except that he would not so limit the customer charge increase for the RTS rate.⁷ He also would adopt the PP&L third block.⁸

In a laudable common sense approach to the complicated, and controversial issues of rate design, the ALJ recognizes that the highly compressed and issue-loaded schedule of this case fails to provide adequate time for a thoughtful examination of rate design issues.⁹

Unfortunately, the rate design issues in this case may not track the broad, long term effects on PP&L's customers between this case and the next likely case, in the 21st century. The extent to which customer charges and block rates affect customer use, and the consequent need for resources, is important. PP&L's proposals guarantee unwise, overuse of supply side resources, and the consequent requirement for the procurement of new supplies, with Pennsylvania customer dollars flowing out of the Commonwealth. By contrast, careful attention now to pricing and rate structure could encourage customers to spend their money here, on demand-side resources, and develop our economy.

⁷ Recommended Decision pp. 230-31.

⁸ Recommended Decision p. 231.

⁹ Recommended Decision pp. 224-227.

EXCEPTION 7: THE ALJ SHOULD HAVE ADOPTED THE SIERRA CLUB PROPOSAL FOR DSM CERTIFICATION AS A CONDITION FOR SECURING AN ECONOMIC DEVELOPMENT RATE.

Sierra Club's Biewald offered the Commission an alternative to the publicly perceived giveaways of economic development rates. He proposed that utility customers seeking to qualify for such rates be certified as having "max'd out" on all cost-effective DSM. But, the ALJ, agreeing with PPLICA's Reply Brief, p. 83, rejects the proposal as going "somewhat beyond the scope of this proceeding" and "relatively untested".¹⁰ An "ongoing investigation into electric utility demand side management programs", presumably the appeal of the Commission's 1993 DSM Order is, says the ALJ, the "better forum".¹¹

The ALJ adopts PP&L's variation on the DSM audit proposal.¹² The PP&L position which he "recommend[s] ... be adopted by the Commission"¹³ provides for:

- a. no rigid requirement that the results must be implemented;
- b. customers should pay for the audits.¹⁴

¹⁰ Recommended Decision p. 246.

¹¹ Recommended Decision pp. 246-47.

¹² Recommended Decision p. 259, citing PP&L Brief, p. 287.

¹³ Recommended Decision p. 259, citing PP&L Brief, p. 287.

¹⁴ See PP&L Brief p. 287. PP&L argues:

Mr. Biewald cites to requirements in a number of New York discount contracts that mandate DSM audits, and recommends similar requirements for the Company's "discount plans," apparently including EDI/IDI credit programs. The New York utility cases described in his exhibits are quite different from the programs at issue in this case, and he made no attempt to relate the theory and reasoning of the New York Commission to the issues before this Commission. Therefore, the general proposition advanced by Mr. Biewald is simply unsupported.

Nonetheless, the Company would not object to requiring companies to perform or present DSM audits as part of the EDI/IDI process, with two caveats as to Mr. Biewald's proposal: (1) there should be no rigid requirement that all of the results of the audit be implemented, because of the balancing of needs for capital projects, and (2) the customers should pay for the audits (PP&L St. 8-r, p.43).

The ALJ, and PPLICA, misconstrue the nature of the proposal. The PP&L position, while positive, is incomplete, because it fails to address the core of the proposal -- insuring equity to all stakeholders and the most efficient use of resources.

The essence of the proposal is that ALL parties share in an effort to maintain a presumably valuable customer's business, the utility, the customers, and the particular customer seeking the beneficial rate. The benefiting customer must undertake only COST-EFFECTIVE energy efficiency measures.

The proposal is flexible, not rigid. The Commission is NOT asked to review and approve another type of DSM program. Rather, the industrial (or other¹⁵) customer, would be free to obtain certification from any appropriate source, utility or non-utility that ANY provider had installed the energy efficiency measures -- the utility, a third party, like a service company (sometimes called "ESCO"), or the customer itself. The certification would be that all COST-EFFECTIVE energy efficiency measures would have been installed.

While the Commission could, in the instant case, specify the meaning of "cost effective", we recommend that the matter be left to an informal negotiation involving customer representatives (including the OCA and interested parties to the instant case), the utility, and CEEP. CEEP would be asked to approve the certification scheme as presumptively valid to put it into effect. Parties disagreeing with the arrangement would have the burden of showing the Commission in a complaint proceeding that the arrangement was unlawful or otherwise unduly discriminatory.

The proposal is affordable, with DSM measures underwritten by the private sector, not utility company customers. Because a definable payback underpins the requirement -- the meaning of cost-effective -- either the customer can finance with internal cash or a commercial lender will finance. Indeed, to the extent that PP&L can help secure low cost financing for the

PP&L Brief p. 287, § VIII.C.6.a.(3) "Implementation of Customer DSM Audits Should Not Be Preconditions to EDI/IDI Program Participation".

¹⁵ While we agree with that part of PPLICA's argument that energy audits be required for other customer groups receiving such discounts, *see* PPLICA Brief p. 83, our proposal focuses on the proposal in this case for an industrial discount. If commercial or residential customers are to become eligible for economic development-type rates then they should follow the same procedures.

customer's energy-related resource, due to the \$2.7 billion utility's market power, the DSM investment can fund itself through bill savings. Thus, the customer benefiting already from an economic development rate should not have to look to the utility or the other customers to underwrite the cost of cost-effective DSM.

There is the added benefit that Mr. Biewald addressed -- there are fewer rate costs to allocate. The ALJ resolves the OCA's sharing proposal dispute in PP&L's favor, allocating costs of the discount to all of the customers.¹⁶ But, to the extent that the industrial customer sees a bill reduction by reason of the DSM (which investment its banker funds), the customers and the shareholders will not be picking up costs of the rate discount. In the ALJ's terms, there will be less of a burden to the "captive customer".¹⁷

The proposal should be simple to administer. By way of example, CEEP could be asked to approve a one-page rider to the economic development rate that provided that:

- (1) a person who could certify the energy efficiency work be a member of a nationally recognized body and not be an employee of the customer seeking the rate;
- (2) the period for determining cost effectiveness, the payback period, be the projected life of the customer's special rate;
- (3) the measures to be certified must be installed and operational by some number of months after the new rate service is provided;
- (4) the certifier would periodically review the installed measures and report to the utility on their effectiveness;
- (5) the utility could cancel the rate after showing bad faith on the customer's part, as by the customer's refusing to place into effect the proposed measures.

¹⁶ Recommended Decision p. 260.

¹⁷ Recommended Decision p. 260.

But none of these elements need be decided in the Commission's order in this case. The Commission need but provide the general policy direction, that an economic development rate can be offered only if the customer is certified to all cost-effective energy efficiency measures per the CEEP-mediated process described above.

EXCEPTION 8: THE RD FAILS TO TAKE A POSITION ON THE BIEWALD SYSTEM BENEFITS PROPOSAL; THE COMMISSION SHOULD ADOPT THE PROPOSAL AS A TIMELY PRELUDE TO THE NEXT FEW YEARS' INDUSTRY CHANGES TOWARD COMPETITION.

The RD does not really address Sierra Club's system benefits charge proposal. Mr. Biewald recommended that the Commission create a "system benefits charge" on each kWh distributed by the utility, folding in those programs and resources that uniquely benefit local customers. He recommended the charge cover DSM, low income programs and other environmental costs.

The RD never considers the proposal. Rather, the ALJ simply mentions the Biewald system benefits charge testimony in passing, and inappositely, in a section of the RD entitled "J. Demand Side Management."¹⁸ Although the proposal does not relate to the various DSM proposals, the RD appears to fold the testimony into a recommendation to "offer no modifications" to the "various alternatives to the current PP&L program, as outlined in this proceeding."¹⁹ This Exception interprets the language as a denial of the proposal, per the RD's blanket statement in the Conclusion.²⁰

The Commission should address the Biewald proposal and adopt it. If, as the Commission anticipates, there are changes coming to the Commonwealth's electric utility industry, and if, as the Company stated, PP&L will not be back before the Commission in a general base rate

¹⁸ Recommended Decision p. 263-65.

¹⁹ Recommended Decision p. 265.

²⁰ Recommended Decision p. 279., § XI. Conclusion, ¶ 6: "That the complaints filed by other parties ... are granted or denied to the extent consistent with the Recommended Decision."

case until after the turn of the millennium, this is the time for the Commission to structure PP&L's rates to absorb the industry changes.

COMMONWEALTH OF PENNSYLVANIA
BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility)
Commission)
)
) Docket No. R-00943271
)
v.)
)
Pennsylvania Power & Light Co.)
(General rate increase request))

EXCEPTIONS OF SIERRA CLUB

SUMMARY

These Exceptions address the following matters:

The ALJ ruling excluding DSM testimony; DSM incentives and lost revenue recovery; economic discount rates and required self-funding DSM programs to cut the losses; a system benefits charge; ending the ECR; customer charges; environmental remediation costs; PP&L low income and energy efficiency programs; and nuclear decommissioning; and the relief Sierra Club has requested.

Attachments are those provided to the parties with Sierra Club's Brief. In the interest of eliminating unnecessary paper they are incorporated by reference here, with copies provided only to the OSA and the Secretary.

HISTORY OF THE CASE

Discussions of the following procedural history of the case, with citations to the record, may be found in Sierra Club's Brief and Reply Brief.

cost, and the schedule be adjusted accordingly. At its June 22, 1995, meeting the Commission denied the request, and Secretary Alford, by sealed letter that day, notified the parties of the Commission decision.

8 RECOMMENDED DECISION

The ALJ issued his 279-page Recommended Decision on July 31, 1995. His cover letter provided that an original and nine copies of any signed Exceptions had to be filed with the Secretary of the Commission, and in the hands of the Office of Special Assistants, Room 210, and the parties by August 14, 1995.

ARGUMENT

1 PROCEDURE: EXCLUDED DSM TESTIMONY

EXCEPTION 1: THE ALJ SHOULD HAVE INCLUDED THE SIERRA CLUB DSM TESTIMONY AS RELEVANT TO SETTING PP&L RATES.

Sierra Club offered the expert testimony of Bruce Biewald on the technical basis for, and design of, DSM incentives and lost revenue recovery. Per the Commonwealth Court's recent decision, a general rate case is the only forum in which to address incentives for DSM, and one of the two forums in which to address the basis for lost revenue recovery. The Sierra Club testimony responded directly to the Court's posturing of the DSM Order.

Bruce Biewald, of the Tellus Institute in Boston, is an MIT grad with 15 years' experience in utility systems planning.²⁸ Mr. Biewald has testified in dozens of regulatory proceedings on

²⁸ Sierra Club Statement 1 (Biewald) pp. 2-3, Sierra Club Ex. 1A-1B.

energy issues and has consulted for business, government, consumer advocate and environmental clients.²⁹

On motion, the ALJ excluded the Biewald DSM testimony. The ALJ denies Sierra Club's Brief's request for reconsideration and reaffirms his initial decision.³⁰ We recognize that, once having made the interlocutory ruling excluding the DSM testimony, the ALJ had no duty to further address the matter of certify it to the Commission for expedited review. Thus, these Exceptions are the appropriate place to seek the Commission's review of the DSM testimony exclusion.

We request that the Commission reverse, and remand within a limited phase of this docket the issues which the excluded testimony presents. This is fair, since principal parties to this case, PPLICA, PP&L, and the OCA opposed even the creation of a separate record at the time.

1.1 THE COMMISSION SHOULD REVERSE THE ALJ'S EXCLUSIONARY RULINGS ON DSM AND CONSIDER THE PROFERRED TESTIMONY ON INCENTIVES AND LOST REVENUES.

Sierra Club hereby incorporates by reference its arguments made on the record with respect to the referenced rulings excluding portions of Mr. Biewald's testimony and denying creation of a separate record for the excluded testimony.

We ask the inclusion of the excluded Biewald testimony and adoption of his proposals. In the alternative we request the reopening of the record to permit the cross examination of Mr. Biewald, by telephone (because his office and home are in Boston), or by deposition, to be placed in the record. The excluded direct testimony is already in the docket file, of course.

If the Commission reverses the exclusion, as we request, and any party seeks cross examination, the record will have to be reopened at that time. That would lengthen these

²⁹ Sierra Club Statement 1 (Biewald) pp. 2-3, Sierra Club Ex. 1A-1B.

³⁰ Recommended Decision pp. 262-65, 275-76.

proceedings unnecessarily. However, there is an easy solution to the time question. In reply to this Sierra claim, the interested parties could state to the Commission whether they would waive such a reopening of the record, agreeing to the testimony coming into evidence without cross examination, should the Commission reverse.

We ask the Commission to note that we have taken every step appropriate to accommodate the schedule in this case. If the testimony is admitted, the parties seeking to cross examine should be required to offer a method that (1) saves Sierra Club harmless from the expense of flying Mr. Biewald back into Harrisburg and paying for his time, approximately \$1,000 for time and expenses, and (2) offers the least disruption to the already extremely tight schedule.

1.2 THE COMMISSION SHOULD ADDRESS INCENTIVES AND LOST REVENUES NOW.

The Commission should address DSM cost recovery in this case, because the opportunity for addressing PP&L incentives and lost revenues may not come until another rate case in the next century. With respect to demand side management ("DSM") expenditures and expenditure levels the Commission should:

- allow direct cost recovery for reasonable and prudent programs;
- allow incentives for reasonable administration of prudent programs, calculated according to the spread embedded in the pricing of PP&L's off-system sales;
- allow the recovery of lost revenues associated with the DSM programs, according to just and reasonable measures;
- require the implementation of programs to secure all cost-effective DSM, as measured by the TRC test;

- require the Company to use all cost-effective DSM means to reduce uncollectible accounts expenses³¹.

Mr. Biewald attempted to testify as to the appropriate method for addressing these matters while the DSM Order of the Commonwealth Court is subject to a petition to review in the Pennsylvania Supreme Court. On motion of the industrial customers, and with OCA and Company support, the ALJ excluded the testimony. If the testimony had been allowed and adopted, the Commission would have provided PP&L's customers with a choice in energy services -- the opportunity to secure cost effective DSM.

The law is that the Commission can only set up a DSM incentive mechanism in a full rate case. Until and unless the Supreme Court grants allocatur, the Commonwealth Court decision on the Commission's December, 1993, DSM Cost Recovery Order is the law. The Opinion provides that the Commission can find and set up DSM incentives only within the context of a full-blown cost of service review in a rate case. Given PP&L's prediction that the Commission will not see it for another general base rate case until after the turn of the millennium, the instant case is the best opportunity for the Commission to do what it ordered in its 1993 DSM cost recovery order -- decide upon a level of DSM incentive payments that will attach to a reasonably and prudently run and Commission-approved DSM program.

This is the Commission's best opportunity to address apparently implied weaknesses in its lost revenue recovery justification. The Commonwealth Court decision also provides the Commission with the opportunity to address the facts and the law supporting DSM lost revenue recovery in a remand proceeding or in a general rate case. It appears that the Commonwealth Court was implying that the Commission 1993 Order had failed to provide the Court with a complete justification of the lost revenue scheme.

The instant case presents an excellent opportunity to address the lost revenues issue -- to "road test" it. The case is already opened and noticed, with all the parties who would address the matter for PP&L's rates in a generic case, anyway. The Company, OTS, OCA,

³¹ See, e.g., PP&L Rate Filing, Statement of Reasons at Book Statement B-4, p. 5 of 6, Statement of Operation and Maintenance Expenses, acct line 904, Customer Accounts Expenses, Uncollectible accounts \$16,932,000.

OSBA, low income advocates, industrial customers and environmental representatives were parties to the DSM cost recovery generic proceedings.

There is a strong tactical reason for the Commission's addressing lost revenue recovery in the instant case. As a matter of tactics, the industrial customer group, which was the principal antagonist to the DSM Cost Recovery Order, stands only to gain by manoeuvring the lost revenues legal debate into a generic case and away from this case. They can take one "shot" at the Commission's legal analysis of lost revenue recovery in an inevitable appeal of the generic decision. By contrast, if the Commission permits the legal and factual debate on lost revenue recovery to go forward in the instant docket, it has an opportunity to examine the industrials' attack in this limited, one-company, context. Then, if a generic or other case(s) is to be held, the Commission can correct any weaknesses the industrials would have attacked in an appeal of a PP&L order.

Thus, the Commission should reverse the ALJ's exclusionary ruling, permit cross, any rebuttal and any surrebuttal in a manner that will not prejudice Sierra Club, and take briefs on the DSM cost recovery issues. Then, as we will argue on supplemental brief, the Commission will have the power and the evidentiary basis to establish a complete DSM cost recovery mechanism for PP&L.

2 EXPENSES

EXCEPTION 2: THE RD SHOULD HAVE RECOMMENDED FULL FUNDING OF ENVIRONMENTAL REMEDIATION BECAUSE CLEANING UP OR AVOIDING POLLUTION IS A COST OF PROVIDING POWER.

The Company sought a \$5.4 million adjustment (\$4.4 million jurisdictional) for environmental remediation. OTS opposed the figure as too high, and in excess of a \$5.0 million per year settlement with the DER (now the "DEP"). The ALJ adopted OTS' "modest" \$400,000 per year adjustment as tracking a DER settlement that took place during this case's litigation.³² While the adjustment seems to track the settlement it provides the

³² Recommended Decision pp. 64-65. Table II to the RD suggests that the ALJ scaled back his disallowance to a jurisdictional \$326,000.

wrong signals to management, and may not track the realities of environmental cleanup costs.

As we did below, we recommend that the environmental remediation be treated as a fund for ratemaking purposes. If the Company's reasonable and prudent expense level is \$400,000 in excess of its settlement because the settlement is a floor, not a ceiling, on such expenditures, the Commission should not force the shareholders to cover legitimate costs engendered through service to the customers. A fund approach will ensure the expenditures go where intended, which appears to be part of OTS' concerns.

2.1 THE COMMISSION SHOULD APPROVE FULL FUNDING OF ENVIRONMENTAL REMEDIATION BECAUSE THE POLLUTION WAS A COST OF PROVIDING POWER.

There is no controversy that the Company will have to fund environmental clean-up costs pursuant to an agreement with DER (soon to be renamed DEP, Dept. of Environmental Protection).³³ The Company may have to clean up as many as 134 sites.³⁴ The issues which PP&L's claim for clean-up expense treatment presents is really whether its clean-up responsibilities are legitimate costs of service, and the amount.

No party claims that environmental clean-up from activities related to the production and supply of power to the customers is other than a legitimate ratemaking expense. Indeed, to fail to recognize these expenses in the cost of service would understate the true cost of the power.

The Company claims its likely annual costs will be \$5.4 million, or \$4.4 million on a jurisdictional basis.³⁵ The scope of the work is defined in the DER agreement on which the estimate must rest. We urge the Commission to adopt this figure, but to do so in a manner

³³ PP&L Statement 2R , pp. 2-3. (Berish); PP&L Ex. MJB-10.

³⁴ PP&L Statement 2R , pp. 2-3. (Berish)

³⁵ PP&L Statement 2R, p. 2. (Berish)

that assures the funds are actually spent for the purposes stated, rather than being folded into general rates, and corporate profitability.

The Commission should require annual reporting of the environmental remediation costs, with budgets and comparisons between budget and actual figures. If, as is common in the field, the cost of remediation substantially increases, the Company should be given the opportunity to return for a revision of the figure. If the cost of work turns out to be significantly less, or the period of the work significantly less than the next base rate case review, other parties should have an opportunity to petition the Commission for a related rate reduction.

We urge the Commission to conclude that, on balance, the Company should undertake fund accounting for this item. Fund accounting, we acknowledge, does not always produce the most cost-effective solutions; there is a tendency for managers to spend up to fund limits because the savings would not otherwise increase corporate profitability. However, the public which is funding these expenditures should know that (a) the rate increase has a public purpose to it, and (b) the funds will go to the purpose the Commission intended -- environmental remediation. Accounting for the approved revenues in an internal Company-managed fund, will provide the necessary assurances.

EXCEPTION 3: THE RD SHOULD HAVE RECOMMENDED TERMINATING THE COMPANY'S ECR IN ORDER TO FOSTER THE MOST ECONOMICALLY EFFICIENT PURCHASES OF ENERGY RESOURCES.

The Company case, of course, supported continuation of the ECR for fuel and power costs. Responding to PP&L's proposal to expand the use of the clause when some capacity reverts to it, we urge the Commission to reject the further use of the clause as providing an unnecessary subsidy to fossil fuels at a time of fuel price stability and increasing competition. The ALJ supports continuation of the ECR, noting that it avoids more frequent rate proceedings and has appropriate checks, and recommends adoption of PP&L's alternative proposal for its JCP&L capacity return.³⁶

³⁶ Recommended Decision pp. 268-73, citing PP&L Brief pp. 294-95 and PP&L St. 7-R, pp. 34-35 (Kleha).

There is no compelling reason to retain the ECR if the Commission is serious about posturing the Commonwealth's utilities for a more competitive environment. The ECR gives them an unfair advantage over other providers, and other sources, of energy. Indeed, by shielding the utility from cost pressure, and therefore cutting back on the frequency of general rate cases, as the ALJ recognized, the clause makes it harder for the Commission to keep track of the overall performance of Pennsylvania's utilities during these changing times.

At the very least, the ECR should be thrown into "the pot" of regulatory changes that the Commission considers in moving Pennsylvania toward more electric competition. Perhaps, in the alternative, the Commission should put PP&L on notice that the ECR may not survive until PP&L's next planned rate case. However, the more forthright action would be to eliminate the clause now, and propel PP&L management immediately toward the more exacting standards of resource procurement in a competitive environment.

2.2 THE COMPANY'S ECR SHOULD TERMINATE IN ORDER TO FOSTER THE MOST ECONOMICALLY EFFICIENT PURCHASES OF ENERGY RESOURCES.

The ECR is a benefit to the Company, not a right. It, in fact, functions as a subsidy to the use of the covered energy sources because it lessens the Company's risk in relying upon them.

ECR treatment of power purchases and fuel expenses should be denied unless the Company can demonstrate that it has maximized the benefits of wholesale market purchasing for its customers, and, in particular, that its purchases are the product of least cost competitive bidding or its substantial equivalent conducted at arms' length from intra-Company sources and affiliates and extra-Company sources.

The proposed treatment of the JCP&L contract termination through the ECR should be denied until and unless the Commission can find that the Company has complied with new competitive bidding regulations in dedicating the capacity and energy for its customers.

EXCEPTION 4: THE RD FAILS TO RECOMMEND THAT CUSTOMER AND COMMUNITY NEEDS PROGRAMS BE ADEQUATELY FUNDED; THEY CONTRIBUTE BENEFITS TO THE PP&L SYSTEM.

PP&L has responded to the responsibilities attendant upon its unique market and life-sustaining position in the Commonwealth by proposing "social" programs that increase the affordability of electric service to its customers. OTS, primarily, opposes the programs on, *inter alia*, the theoretical ground that the programs are not part and parcel of service to the customers. With CEO and Sierra Club, among others, supporting such PP&L programs, and recommending augmentations, the ALJ rejects the OTS adjustments, "giving PP&L the benefit of the doubt" as to the ratemaking, as opposed to the social, utility of the programs.³⁷ We except to the RD only to the extent that the ALJ failed to recommend CEO's enhancements and our suggested reporting mechanism.

2.3 CUSTOMER AND COMMUNITY NEEDS PROGRAMS SHOULD BE ADEQUATELY FUNDED BECAUSE THEY CONTRIBUTE TO THE PP&L SYSTEM.

There should be little doubt by the end of the 20th century that reasonable and prudently incurred utility costs include the type of small customer and community needs programs that PP&L contemplates funding: Build-A-Neighborhood; Affordable Housing; Small Business; Keep Warm; Payment Protection; Winter Emergency; Operating HELP; and CARES' pilot.³⁸ PP&L seeks rate recovery only for the conservation, efficiency, and load management programs, \$3.5 million.³⁹ Thus, the expenditures sought to be covered directly enhance PP&L's ability to deliver cost-effective energy services to ALL its customers.

The programs are traditionally recognized as compensable through the rates. Indeed, for a utility the size of PP&L, and the great geographical breadth of its service territory, the \$3.5

³⁷ Recommended Decision pp. 72-80, 80.

³⁸ PP&L Statement 11, pp. 14-27 (Stathos); OTS Statement 4, p. 32; OTS Main Brief pp. 72-84.

³⁹ PP&L Statement 11, p. 30, 11R p. 11 (Stathos)

million ratepayer cost of the programs is trivial. We do not claim that these programs offer a complete solution to the Company's uncollectibles expense level, or the amount of high-cost peaking power that must be secured annually from other utilities. They do, however, contribute to minimizing these costs.

We share the concerns of the Commission for Economic Opportunity that PP&L's proposals are too narrow, too geographically limited, and underfunded.⁴⁰ One solution is NOT to spread already limited funds over a broader geographic region. Rather, fairness to PP&L's customers implies that funds be allocated to qualifying customers across the system and that PP&L "ramp up" its funding. The Commission should hold that the failure to do so is unreasonable and imprudent. Those funds that are available should be allocated on clear cost-effectiveness criteria.

We also agree that PP&L should not limit its programs to peak-shaving. The Company is incorrect if it believes that attacking baseload inefficiencies fails to benefit the other customers⁴¹. Helping low income customers cut baseload, as with the type of refrigerator change-outs recently announced between PASNY and the New York Housing Authority,⁴² also helps cut bad debts.

Whether the Build-A-Neighborhood and Affordable Housing Programs' funding should issue as block grants is probably best left to determination after Company discussions with affected community groups, with articulated goals and strategies. We hope that the intent is not to reinvent the proverbial wheel, however. There are some very exciting, and successful, affordable housing efforts around the country upon which PP&L staffers can draw. Because the information from these programs should be transferable to other utility service territories we urge the Commission to require PP&L to keep CEEP in the chain of communication, so that the office might informally evaluate the programs' lessons.

⁴⁰ CEO Statement 1, pp. 5-11. (Kuennen)

⁴¹ PP&L Statement 11R, p. 19 (Stathos)

⁴² "Public Housing Efficiency Plan, Step One: Get New Refrigerators", NEW YORK TIMES, "Metro Section" (Jun. 20, 1995), p. B1.

Indeed, the Commission has approved the funding of economic development programs, and economic development rate breaks, with far less certainty of benefit.⁴³ LIURP offers benefits to all customers through targeted low income programs. *See* 52 Pa. Code §§ 58.1-.18. OTS' initial position, rejecting the programs because their benefits are "not[t] identifiable"⁴⁴ would, if adopted, place a special burden on these programs that no others must carry. Nothing, of course, is known in advance, nothing identifiable with certainty.

To the extent that OTS argues that such programs are "social programs" and inappropriate for ratemaking, the claim is wrong, and unfair to both PP&L and its targeted customers.⁴⁵ First, these programs offer traditional economic and financial benefits to the prudent management of an integrated utility system. Second, the argument is unfair to PP&L. The utility, unlike a freely competitive, and mobile, firm, is "stuck" with its customers. In order to have a fair opportunity to earn limited authorized rate of return, it must be given the freedom to develop solutions to serving ALL of its customers in order to retain them and profit from their purchases. Finally, the customers targeted for these programs are "stuck" with PP&L. Because they can go to no other supplier for their electricity, the Commission has an obligation to configure rates to serve them. In utility ratemaking parlance it would be "unjust and unreasonable" to deny ratemaking treatment for these programs to captive customers, particularly in light of the bill-reduction strategies available to large industrial customers through economic development rate discounts.

We share OTS' concern that the programs may be "driven" by PR considerations rather than a judgment that they are good for the system⁴⁶. But the issue is not motive; frequently people and corporations do the right things for the wrong reason. The issue is whether the programs can enhance the services provided to PP&L's customers, particularly those who would turn into bad debt statistics without the programs.

⁴³ *See* PP&L docket no's R-943238(1994); R-00922363 (1992); R-870060C001 (1987); R-850251C001 (1987); R-832542 (1984). *See also* PA. PUC v. NAT'L FUEL GAS DISTR. CORP., 69 Pa. PUC 379, 382 (1989).

⁴⁴ OTS Statement 4, pp. 36-39 (Weakley); OTS Main Brief, p. 82.

⁴⁵ OTS Main Brief pp. 72-84.

⁴⁶ OTS Main Brief, p. 74, citing OTS Statement 4, p. 36 (Weakley).

We fail to see the "unreasonable rate discrimination" that OTS argues⁴⁷. These customer assistance programs are no more discriminatory than any service a utility provides that responds to the needs of a particular customer, or group of customers. In this case the customers happen to be poor ones, who would constitute an economic burden on the system if creative solutions are not found to their payment problems. OTS's argument, if accepted, would simply cast these customers off the system. PP&L's solution seeks to retain them as valued contributors to system costs.

While some reporting and monitoring of these programs is a good idea⁴⁸, and the Company has volunteered to provide some reporting⁴⁹, we urge the Commission to insure that limited funds are spent doing good instead of doing reporting. The CEEP Bureau has spent over a year in a broad collaborative of utility-PUC-customer groups in devising a balance for the need to monitor DSM programs with reporting's potential cost-ineffectiveness. The recent CEEP 100-page report⁵⁰ should serve as a model for reporting on PP&L's programs.

EXCEPTION 5: THE RD FAILS TO PROVIDE THAT NUCLEAR DECOMMISSIONING EXPENSE BE INCREASED TO REFLECT FULLY THE COMPANY'S RECENT, CONSERVATIVE RE-ESTIMATES IN ORDER TO INSURE THAT THE MONEY IS AVAILABLE WHEN NEEDED.

While the ALJ agreed to accept PP&L's estimates of increased decommissioning costs for both "hot", or radiological, structures and the other, nonradiological structures, and its financing approach, he rejected the use of PP&L's engineer's contingency factor.⁵¹ While we share the ALJ's concerns that addressing uncertainty should not turn into "overkill"⁵²,

⁴⁷ OTS Main Brief, p. 80.

⁴⁸ See OCA Main Brief, Vol. I pp. 161-62.

⁴⁹ PP&L Statement 11R, p. 14. (Stathos)

⁵⁰ DEMAND-SIDE MANAGEMENT IMPACT AND PROCESS EVALUATION GUIDELINES FOR PENNSYLVANIA UTILITIES (Pa. PUC's CEEP April 1995).

⁵¹ Recommended Decision pp. 81-99, 98-99.

⁵² Recommended Decision p. 99.

and we believe strongly in the shareholders taking responsibility for their management's selection of the nuclear energy resource, we must except on the ground that the PP&L estimate from Mr. LaGuardia has too many built in underestimates. The ALJ's eliminating the contingency simply exacerbates the undercollection situation.

It is simply not in the Commonwealth's interest to underfund the treatment of radioactive poisons with lives of tens of thousands of years. Given the unlikelihood of PP&L's returning for a general rate case until the next century, and the absence of any other mechanism for collecting for nuclear decommissioning costs, this is the last opportunity for this Commission to adjust PP&L's nuclear decommissioning rates for some time.

2.4 NUCLEAR DECOMMISSIONING EXPENSE SHOULD BE INCREASED
TO REFLECT THE COMPANY'S RECENT, CONSERVATIVE RE-
ESTIMATES IN ORDER TO INSURE THAT THE MONEY IS
AVAILABLE WHEN NEEDED.

The Company's decommissioning estimates are too low. The Company has calculated a stream of revenues to cover the total current cost of decommissioning Susquehanna of \$723.8 million in 1993 dollars.⁵³ The decommissioning trust fund is projected to be roughly \$98.3 million by September 30, 1995.⁵⁴ The Company must fully fund the amount necessary to terminate the license at the time of plant shutdown.⁵⁵ Decommissioning is projected to occur on an "overnight" basis at license expiration -- 2022 for Unit 1 and 2024 for Unit 2,⁵⁶ although in fact it will require 10 years for each unit⁵⁷. The PP&L rate proposal is to

⁵³ See PP&L Initial Brief, p. 139.

⁵⁴ See PP&L Initial Brief, p. 139.

⁵⁵ PP&L Statement 13R, p. 14. (LaGuardia) NRC Final Rule "General Requirements for Decommissioning Nuclear Facilities", 53 Fed. Reg. 24018 (June 27, 1988); NRC Regulatory Guide 1.86, "Termination of Operating Licenses for Nuclear Reactors"; NRC Regulatory Guide 1.159 (availability of funds for decommissioning).

⁵⁶ PP&L Statement 13, Ex. TSL-2 p. 2-1. (LaGuardia)

⁵⁷ PP&L Statement 13, Ex. TSL-2, pp. 5-8. (LaGuardia)

increase the annual decommissioning contribution from \$7.126 million (total Company basis) to \$30.042 million (total Company), \$23.570 million (jurisdictional).⁵⁸

OCA argues that the Company has OVERestimated decommissioning costs by including the decommissioning costs of nonradiological structures and equipment in the annual charges.⁵⁹ OCA puts the Company estimate at \$804 million on a total Company basis, and its witness Bridenbaugh recommends a level of \$573.0 million (total Company).⁶⁰ OCA argues that PP&L's funding and disbursement assumptions understate likely earnings.⁶¹ OCA also argues that the NRC funding requirement does not apply to nonradiological portions of the plant.⁶²

Actually, the prospect of such errors offers the Commission an opportunity to hedge the uncertainties associated with the ultimate cost of decommissioning. We urge the Commission to adopt the Company number and require a revisiting of this issue annually.

The Commission's maintaining some control over the ratemaking of nuclear decommissioning will become increasingly important over the next decade, as the costs are re-estimated during a period in which the utility does not return for base rate review. Just as nuclear construction came to dominate PP&L, and other utility, activity over the previous decade, nuclear decommissioning will increasingly come to dominate PP&L's planning as it becomes the utility's single largest capital project. The Commission should open a sub-docket for the ratemaking treatment of PP&L decommissioning.

If anything, Mr. LaGuardia's decommissioning estimates are too conservative. He recognizes that the NRC decommissioning regulations require restoration of the entire site.⁶³

⁵⁸ PP&L Statement 3, p. 20-21. (Bernini); PP&L Ex. Future 1, Sched. D-11. Cf. OCA Statement 6, pp. 23-24 (Catlin).

⁵⁹ OCA Statement 4, pp. 18-20. (Bridenbaugh)

⁶⁰ OCA Statement 4, p. 6. (Bridenbaugh)

⁶¹ OCA Statement 6, pp. 22-24. (Catlin)

⁶² OCA Main Brief, Vol. 1 p. 168, citing Tr. 2084. (LaGuardia)

⁶³ PP&L Statement 13R, p. 3. (LaGuardia)

Given the hazards of the radionuclides embedded in the to-be-decommissioned structures, it is better to err on planning for clean-up of the entire site, than find at the time that "nonradiological" structures have been contaminated in the invasive decommissioning process⁶⁴, but that there is no money collected to correct the problem. Mr. LaGuardia, however, offers an overly optimistic scenario for calculating costs.

First, the trend of his costs is too low. For instance, the Company case acknowledges that the costs involved in nuclear decommissioning have historically increased at a rate well in excess of the general rate of inflation,⁶⁵ while the Company estimate uses merely the 4.0% CPI change rate for its projections.

Second, the annual decommissioning contribution, the rate, is too low because it spreads collections over too many years. Susquehanna will truly be an outlying statistic in the compilation of nuclear plant operating lives if the LaGuardia assumption is correct -- the Bridenbaugh presentation demonstrated that all commercial reactors entering the decommissioning phase so far have been prematurely shut down⁶⁶. As the Company Initial Brief acknowledges, the LaGuardia estimate rests on the licensing life for the calculation of annual contributions.⁶⁷ PP&L has no plans to extend the operating life of the facility.⁶⁸ Thus, the track record for nuclear operating lives is that they are shorter, not longer, than the LaGuardia assumption for licensing life. This suggests that there will be fewer years in which to collect the recommended annual charges, and that, therefore, the fund will be short when the decommissioning work must begin.⁶⁹

⁶⁴ PP&L Statement 13, pp. 37-38. (LaGuardia)

⁶⁵ See PP&L Initial Brief, pp. 137-38, citing PP&L Statement 17R, pp. 3-4 (Chappalcar).

⁶⁶ Mr. Bridenbaugh points out that the commercial projects supplying decommissioning experience have been premature closures. OCA Statement 4, pp. 10-11. (Bridenbaugh)

⁶⁷ PP&L Initial Brief, p. 135.

⁶⁸ OCA Statement 4, Ex. DGB-11 (Bridenbaugh), PP&L Response to OTS-RB-37.

⁶⁹ To the extent that Susquehanna proves not to be commercially competitive, there will be further pressure to shut it down prematurely. See the OCA sealed (for asserted confidentiality) Cross Examination Ex. 21, "Strategy 2000: Positioning Susquehanna SES For A Competitive Environment", and OCA's argument that the document itself constitutes an admission that the Susquehanna plant is highly uncompetitive. OCA Main Brief, Vol. III (scaled), pp. 53-59.

Third, the 18%-19% contingency which Mr. LaGuardia established⁷⁰ is conservative, given the escalations in other plants' decommissioning estimates⁷¹. While OCA's Bridenbaugh offers encyclopedic knowledge of the nuclear industry⁷², the Commission should infer from his well-supported description of the uncertainties of decommissioning cost⁷³ that cost and schedule could far exceed the LaGuardia projections.⁷⁴

Indeed, fourth, while the Company describes Mr. LaGuardia's disposal cost estimate of \$279 per cubic foot as a "fair proxy" and "very conservative",⁷⁵ the logic upon which it rests suggests that it is too conservative. Mr. LaGuardia built his disposal cost estimate on an assumption that a shallow-land facility, as used for current disposal, is the model for the Susquehanna Plant.⁷⁶ Indeed, the Company is left justifying the number with estimates cited from other utilities, estimates approved by their commissions, all but two of which are higher than the estimate which Mr. LaGuardia adopted.⁷⁷ The Company acknowledges that the regional nuclear storage facility at Barnwell will charge at least \$335 per cubic foot for storage.⁷⁸

The imperatives of the regulatory process contribute to the UNDERprojections of decommissioning costs. While the Company has a financial incentive, if not imperative, to project high expense levels, a projection in excess of Mr. LaGuardia's might generate too unpleasant a message to send to the Commission, and detract from other arguments for line item rate increases. The OCA, and other customer representatives, are bound to advocate

⁷⁰ PP&L Statement 13, pp. 22-24. (LaGuardia); OCA Statement 4, p. 23. (Bridenbaugh)

⁷¹ PP&L Statement 13R, pp. 5-6. (LaGuardia)

⁷² Mr. Bridenbaugh's credentials are extensive. OCA Statement 4, pp. 1-3, Ex. DGB-1. (Bridenbaugh)

⁷³ OCA Statement 4, pp. 4, 11, 24-31. (Bridenbaugh) Mr. Bridenbaugh points out that the "reference cases" for commercial reactor decommissioning are still theoretical, and that the commercial projects supplying decommissioning experience have been premature closures. OCA Statement 4, pp. 10-11. (Bridenbaugh)

⁷⁴ PP&L Statement 13R, pp. 6-13. (LaGuardia)

⁷⁵ PP&L Initial Brief, p. 132.

⁷⁶ See PP&L Statement 13R, p. 9. (LaGuardia)

⁷⁷ PP&L Initial Brief, pp. 132-34.

⁷⁸ PP&L Initial Brief, pp. 133-34, citing WALL STREET JOURNAL (June 15, 1995), p. A5.

the lowest reasonable rates; and they may well have legitimate arguments that the shareholders take responsibility for the decommissioning of facilities that the Company's board and management chose to construct.

But our concern is that wastes with half-lives of thousands of years, including the power-generating facilities of the Susquehanna plant, be properly managed. Due to the time value of the collected funds, underestimates today become increasingly hard to correct in the future.⁷⁹ As a society, we must plan for the inevitable mitigation of the nuclear power plant pollution. From society's point of view, intergenerational equity requires that those who benefit from the power generation which produces pollution should pay for mitigating the pollution⁸⁰. Thus, the Commission should adjust rates to reflect the present underassessment for the responsibility to safely dispose of the "hot" portions of Susquehanna.⁸¹

3 RATE DESIGN

EXCEPTION 6: THE RD WOULD SEND THE WRONG PRICE SIGNALS TO CUSTOMERS BY SETTING THE CUSTOMER CHARGE TOO HIGH AND PERMITTING A THIRD BLOCK -- THE RS CHARGE SHOULD BE SET AT \$4.80.

PP&L would substantially raise the customer charge and offer discounts for increased usage through a declining block rate structure. We oppose the increase on the ground that it sends the wrong price signals to customers, and, given the changes likely in the electric utility

⁷⁹ Mr. Bridenbaugh's point regarding the likely continued use of hard-to-find and expensive-to-prepare generation sites. OCA Statement 4, p. 20 (Bridenbaugh), is persuasive. However, the consequences of decommissioning underestimates are so grave that the Commission would be better advised to err on the side of overcollection now, making provision that savings from future site reuse accrue to the benefit of the customers.

⁸⁰ OCA Statement 4, p. 12 . (Bridenbaugh)

⁸¹ To the extent that the Commission considers OCA's powerful arguments on the economic excess capacity which Susquehanna represents, it must take account of the contribution which decommissioning expense makes to the premium which customers pay over "market" for the plant's nuclear power. Then, to the extent the Commission determines that PP&L shareholders must bear some of the cost responsibility for the premium, it may weigh allocating decommissioning cost responsibility to the shareholders. Our concern is that explicit, real contributions be made to the decommissioning fund.

industry until the next PP&L rate case, will constitute an anachronism of monopoly pricing. The ALJ rejects the parties' attacks on the PP&L proposal and recommends, without citation to record support, a 35% increase in the customer charge, except that he would not so limit the customer charge increase for the RTS rate.⁸² He also would adopt the PP&L third block.⁸³

In a laudable common sense approach to the complicated, and controversial issues of rate design, the ALJ recognizes that the highly compressed and issue-loaded schedule of this case fails to provide adequate time for a thoughtful examination of rate design issues.⁸⁴

Unfortunately, the rate design issues in this case may not track the broad, long term effects on PP&L's customers between this case and the next likely case, in the 21st century. The extent to which customer charges and block rates affect customer use, and the consequent need for resources, is important. PP&L's proposals guarantee unwise, overuse of supply side resources, and the consequent requirement for the procurement of new supplies, with Pennsylvania customer dollars flowing out of the Commonwealth. By contrast, careful attention now to pricing and rate structure could encourage customers to spend their money here, on demand-side resources, and develop our economy.

3.1 THE CUSTOMER CHARGE SHOULD BE SET AT \$4.80 BECAUSE A HIGH CUSTOMER CHARGE SENDS THE WRONG ECONOMIC SIGNALS.

The Company maintains its claim for a \$7.20 residential customer charge through the rebuttal phase of the case.⁸⁵ The Commission should view the claim as a throwaway, largely a bargaining chip to be lost in favor of other claims.

⁸² Recommended Decision pp. 230-31.

⁸³ Recommended Decision p. 231.

⁸⁴ Recommended Decision pp. 224-227.

⁸⁵ PP&L Statement 8-R (Kasper rebuttal).

The OCA and CEPFOD positions are fairer, and are grounded in the economics of an industry moving toward the competitive sale of energy services.

The meter, or hookup to the grid, is the least competitive, most monopolistic aspect of all customers' services. Because residential customers, as small customers, have less market power than those of other classes, the Commission has a special obligation to protect them.

A large customer charge sends the wrong price signals to customers. As long as the supply of fuels is limited, and utility distributors would have to secure additional power sources with growing load, there is a benefit to tagging the consumption of kWh's with its true costs. Reasonable and prudently incurred costs for a mature system like PP&L's should attach to the energy component of the customer's bill. The Commission should not increase the customer charge.

Assuming *arguendo* that the Commission alters the customer charge, there is a strong case to spread the costs within each class proportionately to consumption blocks -- the more a customer uses, the more likely (s)he is to pay an increment to the customer charge. (By contrast, simplicity would, of course, require that the charge attach to the customer, not to the consumption block, as PP&L suggests⁸⁶.) The Commission could find that additional costs are trackable to higher consumption residential customers, those in new subdivisions of bigger, air-conditioned or electrically heated houses farther away from population centers. Thus, with consumption divided into blocks, the more a customer used, the greater the customer charge to be paid.

Assuming *arguendo*, again, that the Commission alters the customer charge, there are solid reasons to mate customer charges with consumption. Higher consumption brings with it predictably higher costs, as the distributor must contract for additional firm load. An inclining block structure, be it one for the customer charge or one for kWh consumption, positions the utility's captive customers for the likely restructuring of the Pennsylvania electric utility industry, and PP&L. PP&L customers may well be served by other than a non-vertically-integrated electric distribution company before the next rate case. Inclining block rates will help put off the day when the distributor must secure new, higher cost

⁸⁶ PP&L Statement 8-R (Kasper rebuttal) p. 8.

resources. Indeed, just as "[l]oad management measures need a long-lead time compared to supply side options" (PP&L's Mr. Kasper)⁸⁷, the inclining block customer charge requires the next few years to produce its benefits.

The Company proposal for a declining block customer charge is self-contradictory. The Company's proposal to replace the RTS thermal storage rate with a new tariff incorporating available central load control devices⁸⁸ rests on a recognition that avoiding the acquisition of new peaking resources will cut costs. Similarly, the rate structure for the customer charge, if not the commodity charge, should recognize the extra burden that poor load factor customers place on the system at peak times.⁸⁹

EXCEPTION 7: THE ALJ SHOULD HAVE ADOPTED THE SIERRA CLUB PROPOSAL FOR DSM CERTIFICATION AS A CONDITION FOR SECURING AN ECONOMIC DEVELOPMENT RATE.

Sierra Club's Biewald offered the Commission an alternative to the publicly perceived giveaways of economic development rates. He proposed that utility customers seeking to qualify for such rates be certified as having "max'd out" on all cost-effective DSM. But, the ALJ, agreeing with PPLICA's Reply Brief, p. 83, rejects the proposal as going "somewhat beyond the scope of this proceeding" and "relatively untested".⁹⁰ An "ongoing investigation into electric utility demand side management programs", presumably the appeal of the Commission's 1993 DSM Order is, says the ALJ, the "better forum".⁹¹

⁸⁷ PP&L Statement 8-R (Kasper rebuttal) p. 14.

⁸⁸ PP&L Statement 8-R (Kasper rebuttal) p. 12.

⁸⁹ This operating burden is different from that associated with the Company's past investment in high-capital-cost baseload facilities, in order to meet the requirements of high load factor customers for relatively large amounts of reliable, round-the-clock power. *See* OCA Statement No. 3, Direct Testimony of Dr. Charles Johnson, pp. 9-13.

⁹⁰ Recommended Decision p. 246.

⁹¹ Recommended Decision pp. 246-47.

The ALJ adopts PP&L's variation on the DSM audit proposal.⁹² The PP&L position which he "recommend[s] ... be adopted by the Commission"⁹³ provides for:

- a. no rigid requirement that the results must be implemented;
- b. customers should pay for the audits.⁹⁴

The ALJ, and PPLICA, misconstrue the nature of the proposal. The PP&L position, while positive, is incomplete, because it fails to address the core of the proposal -- insuring equity to all stakeholders and the most efficient use of resources.

The essence of the proposal is that ALL parties share in an effort to maintain a presumably valuable customer's business, the utility, the customers, and the particular customer seeking the beneficial rate. The benefiting customer must undertake only COST-EFFECTIVE energy efficiency measures.

⁹² Recommended Decision p. 259, citing PP&L Brief, p. 287.

⁹³ Recommended Decision p. 259, citing PP&L Brief, p. 287.

⁹⁴ See PP&L Brief p. 287. PP&L argued:

Mr. Biewald cites to requirements in a number of New York discount contracts that mandate DSM audits, and recommends similar requirements for the Company's "discount plans," apparently including EDI/IDI credit programs. The New York utility cases described in his exhibits are quite different from the programs at issue in this case, and he made no attempt to relate the theory and reasoning of the New York Commission to the issues before this Commission. Therefore, the general proposition advanced by Mr. Biewald is simply unsupported.

Nonetheless, the Company would not object to requiring companies to perform or present DSM audits as part of the EDI/IDI process, with two caveats as to Mr. Biewald's proposal: (1) there should be no rigid requirement that all of the results of the audit be implemented, because of the balancing of needs for capital projects, and (2) the customers should pay for the audits (PP&L St. 8-r, p.43).

PP&L Brief p. 287, § VIII.C.6.a.(3) "Implementation of Customer DSM Audits Should Not Be Preconditions to EDI/IDI Program Participation".

The proposal is flexible, not rigid. The Commission is NOT asked to review and approve another type of DSM program. Rather, the industrial (or other⁹⁵) customer, would be free to obtain certification from any appropriate source, utility or non-utility that ANY provider had installed the energy efficiency measures -- the utility, a third party, like a service company (sometimes called "ESCO"), or the customer itself. The certification would be that all COST-EFFECTIVE energy efficiency measures would have been installed.

While the Commission could, in the instant case, specify the meaning of "cost effective", we recommend that the matter be left to an informal negotiation involving customer representatives (including the OCA and interested parties to the instant case), the utility, and CEEP. CEEP would be asked to approve the certification scheme as presumptively valid to put it into effect. Parties disagreeing with the arrangement would have the burden of showing the Commission in a complaint proceeding that the arrangement was unlawful or otherwise unduly discriminatory.

The proposal is affordable, with DSM measures underwritten by the private sector, not utility company customers. Because a definable payback underpins the requirement -- the meaning of cost-effective -- either the customer can finance with internal cash or a commercial lender will finance. Indeed, to the extent that PP&L can help secure low cost financing for the customer's energy-related resource, due to the \$2.7 billion utility's market power, the DSM investment can fund itself through bill savings. Thus, the customer benefiting already from an economic development rate should not have to look to the utility or the other customers to underwrite the cost of cost-effective DSM.

There is the added benefit that Mr. Biewald addressed -- there are fewer rate costs to allocate. The ALJ resolves the OCA's sharing proposal dispute in PP&L's favor, allocating costs of the discount to all of the customers.⁹⁶ But, to the extent that the industrial customer sees a bill reduction by reason of the DSM (which investment its banker funds), the

⁹⁵ While we agree with that part of PPLICA's argument that energy audits be required for other customer groups receiving such discounts, *see* PPLICA Brief p. 83, our proposal focuses on the proposal in this case for an industrial discount. If commercial or residential customers are to become eligible for economic development-type rates then they should follow the same procedures.

⁹⁶ Recommended Decision p. 260.

customers and the shareholders will not be picking up costs of the rate discount. In the ALJ's terms, there will be less of a burden to the "captive customer".⁹⁷

The proposal should be simple to administer. By way of example, CEEP could be asked to approve a one-page rider to the economic development rate that provided that:

- (1) a person who could certify the energy efficiency work be a member of a nationally recognized body and not be an employee of the customer seeking the rate;
- (2) the period for determining cost effectiveness, the payback period, be the projected life of the customer's special rate;
- (3) the measures to be certified must be installed and operational by some number of months after the new rate service is provided;
- (4) the certifier would periodically review the installed measures and report to the utility on their effectiveness;
- (5) the utility could cancel the rate after showing bad faith on the customer's part, as by the customer's refusing to place into effect the proposed measures.

But none of these elements need be decided in the Commission's order in this case. The Commission need but provide the general policy direction, that an economic development rate can be offered only if the customer is certified to all cost-effective energy efficiency measures per the CEEP-mediated process described above.

⁹⁷ Recommended Decision p. 260.

3.2 BIEWALD TESTIMONY: THE COMMISSION SHOULD REQUIRE
MAXIMUM COST-EFFECTIVE DSM AS A PREREQUISITE TO
ECONOMIC DISCOUNT RATES.

We urge the Commission to act, rather than REact, to changes in the electric utility industry. Tellus' Bruce Biewald provided a well-reasoned proposal to protect the integrity of the region's ability to supply reliable, economical and environmentally benign power -- no DSM, no discounts.

The Commission should require as a precondition to eligibility for any promotional or discount rate, including "economic development rates", that a business customer be initially and periodically certified through an approved independent auditor that it has undertaken to cost-effectively maximize the energy efficiency of its operations, as measured for the period that the rate is expected to be in effect for it, OR that it has in place an approved plan for such cost-effective measures. PP&L, and ultimately each other electric utility in the state, must demonstrate that any industrial customer seeking an economic development rate discount use the maximum amount of the cheapest, most environmentally responsible, source of energy services for Pennsylvanians -- cost-effective demand side management -- to lower its bills.

Mr. Biewald made the following conclusions and observations:

Economic Discount Rates - Conclusions

1. Economic discount rates have the potential for creating inequities among customer classes.
2. It is possible to reduce the amount of the rate discount, and therefore any associated inequities, by structuring the tariffs to require participating customers to adopt cost effective DSM measures. An efficiency requirement can be included in the terms and conditions for the discounted rate.
3. To the extent that utility shareholders absorb some of the revenues that are lost as a result of economic discount rates, the utility will have an incentive to minimize the

amount of the discount rate, through negotiations with the customer and with cost-effective DSM programs.

4. It is possible to reduce the inequities created by discount rates by providing all customers with access to cost-effective DSM programs.

Economic Discount Rates - Recommendations

1. The Commission should require that large industrial or commercial customers demonstrate through certified energy audits and proof of work done that they have already implemented, or have made a commitment to implement, maximum cost-effective DSM measures before they may participate in PP&L's discount rate programs.
2. PP&L should be required to minimize the inequities caused by economic discount rates by providing a meaningful option for cost-effective DSM programs to all customers.⁹⁸

There is precedent for the DSM-discount rate proposal. New York requires "independent and comprehensive DSM audits" of industrial customer premises and processes as a condition for eligibility for flexible rates.⁹⁹ New Jersey's recently-adopted Energy Master Plan suggests that the New Jersey Board of Public Utilities include in draft flex rate legislation a requirement that prospective flex rate customers undergo a comprehensive energy audit.¹⁰⁰ Indeed, a NJ Senate bill proposes that, upon application of a utility for a retail discount rate:

3.c(4) Evidence of a comprehensive energy audit of the customer facility must be submitted to the utility prior to the effective date of the discount rate agreement.¹⁰¹

⁹⁸ Sierra Club Statement 1 (Biewald) pp. 7, 25-30.

⁹⁹ Opinion and Order Regarding Flexible Rates, No. 94-15, Case 93-M-0229 (July 11, 1994), p. 31 ¶ 5 (excerpt attached as Sierra Club Att. C).

¹⁰⁰ New Jersey Energy Master Plan (March 1995), p. 26 (excerpt attached as Sierra Club Att. E).

¹⁰¹ N.J. Senate Bill S-1940 § 3.c(4), p. 3 (Proposed 1995) (excerpt attached as Sierra Club Att. F).

The economics for the Biewald proposal are win-win-win; by contrast, the economics for the Company's economic development rate proposal, or the rate it would replace, are largely a loser for all.

The typical economic development rate is a relatively negative, reactive measure. The term is, indeed, a misnomer because nothing is being developed. The rate is a tool to maintain a difficult status quo by simply reducing the industrial customer's bill for a set amount of electricity. Either the utility's shareholders or the other customers absorb the difference in revenues, and the customer's production processes are no more efficient than before. The economic development rate is an economic preservation rate.

The Biewald proposal is a positive one. It enhances economic growth and provides an opportunity for all parties to gain. The net of the industrial customer's DSM+ED rate investment should equal or surpass the standard-operating-procedure rate reduction. The utility winds up offering a more modest rate break, and increased efficiencies at the customer's premises may actually increase production, and kWh sales. The other customers benefit from the increased local economic activity as the industrial customer invests in DSM measures and increases production, if not power purchases, due to increased efficiency.

Indeed, the Commission should require the Company to enhance the choices available to its customers by providing and marketing to ALL classes of customers discounted tariffs, predicated upon the appropriate certification that the customer has engaged, or is engaged actively, in comprehensive DSM activities and investments to cost-effectively minimize the consumption of electricity, including the customer's contribution to class coincident peaks.

EXCEPTION 8: THE RD FAILS TO TAKE A POSITION ON THE BIEWALD SYSTEM BENEFITS PROPOSAL; THE COMMISSION SHOULD ADOPT THE PROPOSAL AS A TIMELY PRELUDE TO THE NEXT FEW YEARS' INDUSTRY CHANGES TOWARD COMPETITION.

The RD does not really address Sierra Club's system benefits charge proposal. Mr. Biewald recommended that the Commission create a "system benefits charge" on each kWh distributed by the utility, folding in those programs and resources that uniquely benefit local

customers. He recommended the charge cover DSM, low income programs and other environmental costs.

The RD never considers the proposal. Rather, the ALJ simply mentions the Biewald system benefits charge testimony in passing, and inappositely, in a section of the RD entitled "J. Demand Side Management."¹⁰² Although the proposal does not relate to the various DSM proposals, the RD appears to fold the testimony into a recommendation to "offer no modifications" to the "various alternatives to the current PP&L program, as outlined in this proceeding."¹⁰³ This Exception interprets the language as a denial of the proposal, per the RD's blanket statement in the Conclusion.¹⁰⁴

The Commission should address the Biewald proposal and adopt it. If, as the Commission anticipates, there are changes coming to the Commonwealth's electric utility industry, and if, as the Company stated, PP&L will not be back before the Commission in a general base rate case until after the turn of the millennium, this is the time for the Commission to structure PP&L's rates to absorb the industry changes.

3.3 BIEWALD TESTIMONY: THE COMMISSION SHOULD REQUIRE A SYSTEM BENEFITS CHARGE AS A COMPONENT OF EACH KWH, TO COVER THE COST OF SUCH BENEFITS TO ALL CUSTOMERS AS LOW INCOME PROGRAMS, POLLUTION CONTROL, AND DSM.

We ask the PUC to create a "system benefits charge" on each kWh distributed by the utility, folding in those programs and resources that uniquely benefit local customers. Mr. Biewald has recommended the charge cover DSM, low income programs and other environmental costs. Regardless of how industry restructuring affects Pennsylvania the Commission should position PP&L and its customers now to protect these valuable programs from retail wheeling bypass.

¹⁰² Recommended Decision p. 263-65.

¹⁰³ Recommended Decision p. 265.

¹⁰⁴ Recommended Decision p. 279., § XI. Conclusion, ¶ 6: "That the complaints filed by other parties ... are granted or denied to the extent consistent with the Recommended Decision."

It now appears that the restructuring debate will extend over a period of years. The Commission could use a near-term strategy that can sustain progress on crucial long-term investments while that debate proceeds. The Biewald recommendation for a system benefits charge addresses the very concern that NARUC recently expressed regarding "potentially stranded benefits".¹⁰⁵

The National Association of Regulatory Utility Commissioners, NARUC, passed a resolution supporting the protection of "stranded benefits" at its November 1994 annual meeting in Reno, Nevada.¹⁰⁶ NARUC concluded that "it is the responsibility of state and federal electric utility regulators to assure that those vital public benefits are not 'stranded', but are well served in new electric industry structures and in the transition to them." These benefits include, according to NARUC:

- "systematic investments in energy efficiency";
- "responsible management of the environmental impacts of electric generation;
- "innovative rate designs ... [in] meeting the specific needs of low-income customers";
- "system reliability and fuel diversity";
- "research and development for the electric industry".¹⁰⁷

Indeed, to the extent that such peak reduction measures as DSM can save PP&L and PJM from, for example, the unforeseen loss of 2,000 MW of the Salem nuclear plant's baseload contribution during the summer peak, they are worth protecting and encouraging. The solution to the stranded investment challenge lies in converting cost recovery for energy efficiency, low-income services and R&D to a non-bypassable, usage-based "system benefits charge" on electric distribution services. Cost-effective renewable energy acquisitions should also qualify to the extent that their initial cost streams exceed short-term commodity costs. This would create a cost recovery structure that can accommodate strong performance-based incentives and retain consistency with all plausible restructuring outcomes.

¹⁰⁵ Sierra Club Statement 1 (Biewald) p. 31.

¹⁰⁶ Sierra Club Exhibit 1E, "Resolution on Competition, the Public Interest, and Potentially Stranded Benefits".

¹⁰⁷ Sierra Club Exhibit 1E.

There is precedent for such a charge in Pennsylvania. Washington's Utilities and Transportation Commission recognized the value of a system benefits charge in its December 14, 1994, meeting, in approving Washington Water Power's proposal for a usage-based distribution charge to recover energy-efficiency investments.¹⁰⁸ Idaho followed in March of 1995.¹⁰⁹

The recommended cost-recovery system requires no change in current rates or rate structures. PP&L and other utilities today typically recover "stranded benefits" charges from all distribution system users based on volume of consumption; they would continue to do so under the new system. The only difference is that the Commission would make explicit (as Idaho and Washington now have) that distribution system users cannot bypass their share of contributions to stranded benefits by designating a new supplier of kilowatthours over the integrated grid (assuming that Pennsylvania ever decided to permit this).

Mr. Biewald came to the following conclusions and made these recommendations:

Recovery of DSM Costs Through a System Benefits Charges - Conclusions

1. As the debate over electric utility industry restructuring has evolved, utilities have become increasingly concerned that price increases due to DSM cost recovery will place them at a competitive disadvantage and encourage large customers to leave the system.
2. Cost-effective DSM programs provide a variety of resource benefits that accrue to *all customers* on the utility system.
3. A "system benefits" charge can be designed to ensure that all customers pay for their share of the DSM program costs, and to prevent uneconomic bypass of a utility

¹⁰⁸ APPLICATION OF WASHINGTON WATER POWER, Docket No. UE-941375, UE-941377 (Minute Order of Dec. 14, 1994, Wash. Utilities and Transportation Com'n), WWP Petition for Tariff Revisions, Schedule 91, "Experimental DSM Rider Adjustment - Washington" (Sierra Club Att. A); WPP Petition WUTC Staff Recommendation for Approval (Sierra Club Att. B); Sierra Club Statement No. 1 (Biewald) p. 33.

¹⁰⁹ Application of Washington Water Power, Case No.'s WWP-E-94-10, WWP-G-94-5, Order No. 25917 (Idaho PUC Mar. 6, 1995) (Sierra Club Att. C).

system. The charge would be "volumetric", assigned on the basis of consumption, rather than a customer, basis.

4. A system benefits charge would enable PP&L to recover all appropriate DSM costs under a variety of future restructuring and competition scenarios, and would not place PP&L at a competitive disadvantage with regard to retail wheeling or self-generation. Appropriately designed, a system benefits charge may also provide the vehicle for this Commission to position Pennsylvania utilities for industry restructuring.

Recovery of DSM Costs Through System Benefits Charges - Recommendations

1. The Commission should establish a non-bypassable system benefits charge for recovering DSM costs.
2. The Commission should establish a DSM cost recovery mechanism which (a) allows PP&L to recover all appropriate DSM program costs, (b) prevents uneconomic bypass, and (c) will be appropriate under a variety of future electricity industry restructuring scenarios.
3. The Commission should make all approved DSM programs, including low income and other DSM programs, subject to the non-bypassable system benefits charge. The Commission should also consider including other utility expenditures in the charge, perhaps those for environmental benefits.¹¹⁰

There should be no federal preemption of a system benefits charge. The Federal Energy Regulatory Commission (FERC) acknowledges state ratemaking authority over distribution services. While the boundary between state-regulated distribution and FERC-regulated transmission may prove to be blurred, there should be no dispute as to the boundary's existence.

In the March 29, 1995 Notice of Proposed Rulemaking, the "MEGA NOPR", FERC explicitly endorsed state and local regulators' right to use distribution charges to avoid

¹¹⁰ Sierra Club Statement I (Biewald) pp. 7-8, 31-33.

"stranded benefits" from utility investments in energy efficiency. The agency confirmed that nonfederal regulators "may also use their jurisdiction over local distribution facilities to address potential 'stranded benefits', e.g., environmental benefits associated with conservation, load management, and other demand side management (DSM) programs."¹¹¹ FERC cited NARUC's resolution on "stranded benefits".¹¹²

We request that the Commission order PP&L to segregate in a system benefits charge its low income, DSM, R&D and other environmental costs, allocating those costs on the same per-kWh formula as it would have without the identified charge.

RELIEF REQUESTED

Sierra Club requests, as relief, that the Commission:

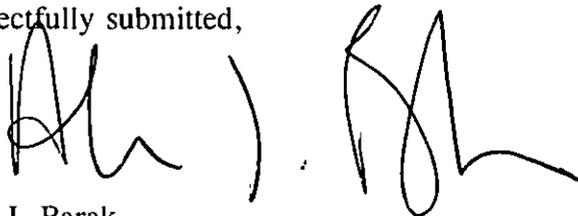
- a. Reverse the ALJ and receive into evidence the Biewald DSM cost recovery testimony;
- b. Deny any increase or change in PP&L's rates that is unjust, unreasonable, unduly discriminatory or inconsistent with the Public Utility Code, sound ratemaking principles, and public policy;
- c. Determine the justness and reasonableness of PP&L's current and proposed rates;
- d. Adopt the recommendations and proposals advocated in these Exceptions;
- e. Grant all other relief to which Sierra Club is entitled; and

¹¹¹ 60 Fed. Reg. 17662, 17691 n. 230, 17711 n. 304 (Apr. 7, 1995).

¹¹² 60 Fed. Reg. 17662, 17691 n. 230, 17711 n. 304 (Apr. 7, 1995).

- f. Grant such other relief which the Commission may deem to be necessary and proper.

Respectfully submitted,



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Dated: August 14, 1995

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COMMONWEALTH OF PENNSYLVANIA
BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility)
Commission)
 v.) Docket No. R-00943271
)
Pennsylvania Power & Light Co.)
(General rate increase request))

CERTIFICATE OF SERVICE

I hereby certify that I have caused on this, the 12th day of August, 1995, to be served a true copy of Sierra Club's Exceptions upon the following parties of record to this proceeding by First Class Mail, as indicated and addressed as follows, except that where indicated I have caused the party to be served by hand on August 14, 1995:

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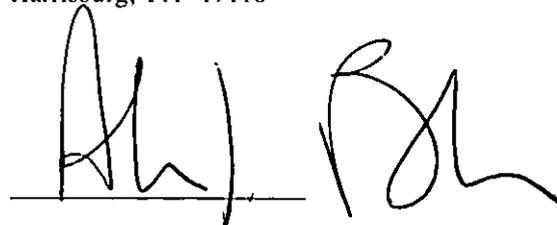
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COMMONWEALTH OF PENNSYLVANIA
BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility)
Commission)
)
v.) Docket No. R-00943271
)
Pennsylvania Power & Light Co.)
(General rate increase request))

INCORPORATED BY REFERENCE:

SIERRA CLUB'S BRIEF

ATTACHMENTS

TABLE OF ATTACHMENTS

- Att A: APPLICATION OF WASHINGTON WATER POWER, Docket No. UE-941375, UE-941377 (Minute Order of Dec. 14, 1994, Wash. Utilities. and Transportation Com'n), WWP Petition for Tariff Revisions, Schedule 91, "Experimental DSM Rider Adjustment - Washington"
- Att B: WPP Petition WUTC Staff Recommendation for Approval
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- Att E: New Jersey Energy Master Plan (March 1995), p. 26 (excerpt)
- Att F: N.J. Senate Bill S-1940 § 3.c(4), p. 3 (Proposed 1995) (excerpt)
- Att G: Excluded testimony of Bruce Biewald on DSM Cost Recovery

NOTE: ATTACHMENTS PROVIDED TO OFFICE OF SPECIAL ASSISTANTS.